MONEYGRAM INTERNATIONAL INC
Form 425
December 18, 2007

Filed by Euronet Worldwide, Inc.

Pursuant to Rule 425 under the

Securities Act of 1933, as amended

Subject Company:

MoneyGram International, Inc.

(Commission File No. 001- 31950)

On December 18, 2007, the following statement was issued on behalf of Euronet Worldwide, Inc.:

Euronet welcomes the views of all MoneyGram shareholders and is pleased that Blum Capital, a large and well-respected shareholder, has echoed Euronet s call for MoneyGram to negotiate with us in good faith consistent with their fiduciary duty to maximize shareholder value. We have delivered to MoneyGram a mark up of their draft confidentiality agreement that we are prepared to sign today that would protect confidential information while allowing us to continue talking directly to MoneyGram shareholders, but eliminate the onerous standstill restriction. We believe we have already made a compelling offer and we remain willing to consider raising it should MoneyGram provide non-public information that would justify an increase. The ball is now in MoneyGram s court - if they are sincere in their expressed willingness to meet with us, they will immediately execute the agreement and begin negotiations.

FORWARD-LOOKING STATEMENTS

This communication contains forward-looking statements, including statements regarding Euronet Worldwide, Inc., MoneyGram International, Inc., and the combined company after the completion of the proposed transaction between Euronet and MoneyGram. These statements include, but are not limited to, statements about the anticipated consequences and benefits of the proposed transaction, including future strategic and financial benefits, the plans, objectives, expectations and intentions of Euronet following the completion of the proposed transaction and other statements that are not historical facts. These statements are based upon the current beliefs and expectations of Euronet s management and publicly available information about MoneyGram, and are subject to significant risks and uncertainties. Actual results may vary materially from those anticipated in such forward-looking statements as a result of a number of factors, including: the failure of MoneyGram to accept Euronet s proposal; the failure to consummate any transaction agreed to between Euronet and MoneyGram or to consummate any such transaction in the expected timeframe; the risk that the opportunities and synergies anticipated to result from the proposed transaction may not be fully realized or may take longer to realize than expected; conditions imposed with obtaining governmental approvals and rulings on or regarding the transaction; the risk that the businesses of Euronet and MoneyGram will not be integrated successfully; disruption from the proposed transaction making it difficult to maintain relationships with employees, customers or other third parties with which we do business; technological developments affecting the market for Euronet s or MoneyGram s products and services; foreign exchange fluctuations; and changes in laws and regulations affecting Euronet s or MoneyGram s businesses. Additional risks are described in the Euronet s filings with the Securities and Exchange Commission (SEC), including its Annual Report on Form 10-K, Quarterly Reports on Form 10-Q and Current Reports on Form 8-K. Copies of these filings may be obtained as described below.

ADDITIONAL INFORMATION

This communication is neither an offer to exchange nor a solicitation of an offer to exchange any securities of MoneyGram. The exchange offer (the Exchange Offer) for the outstanding shares of MoneyGram common stock described in this communication has not commenced. In connection with the proposed transaction, Euronet intends to file relevant materials with the Securities and Exchange Commission (the SEC), such as a Registration Statement on Form S-4, a Tender Offer Statement on Schedule TO (including a prospectus-offer to exchange, a letter of transmittal and other offer documents) and a proxy statement (collectively, the Offer Documents) and any offers or solicitations will be made only pursuant to the Offer Documents filed with the SEC. Investors are advised to read carefully and in their entirety the Offer Documents that are filed with the SEC when they become available because they will contain important information.

Euronet and its directors, executive officers and certain other employees and representatives of Euronet may be considered participants in a solicitation of proxies in connection with the proposed transaction. Information about Euronet s executive officers and directors is available in Euronet s proxy statement, dated April 11, 2007, for its 2007 annual meeting of stockholders. Additional information about the interests of potential participants in a solicitation will be in the Offer Documents, when they become available, and other relevant documents filed with the SEC.

Euronet and MoneyGram stockholders may obtain copies of the Offer Documents and other relevant documents filed with the SEC for free, when they become available, at the SEC s website at www.sec.gov or by calling Innisfree M&A Incorporated, the Information Agent for the Exchange Offer, toll-free in the U.S. and Canada at 1-877-456-3488 or toll-free in Europe at 00 800 7710 9970.

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32,871

66,479

3,623

32,516

215,312

Balance, ending

$

14,207,733

$

12,999,233

$

2,638,301

$

2,430,454

$

1,080,911

$

33,356,632

The allowance by impairment evaluation and by portfolio segment as of June 30, 2018 and December 31, 2017 is presented as follows:

As of June 30, 2018

	C&I	CRE	Direct Financing Leases	Residential Real Estate	Installment and Other Consumer	Total
lowance r impaired ans/leases	$ 308,091	$ 2,109,374	$ 375,803	$ 239,419	$ 106,878	$ 3,139,565
lowance nimpaired ans/leases	14,925,780	13,709,666	2,348,552	2,193,683	1,227,830	34,405,511
	$ 15,233,871	$ 15,819,040	$ 2,724,355	$ 2,433,102	$ 1,334,708	$ 37,545,076
paired ans/leases	$ 1,551,445	$ 6,967,425	$ 2,529,004	$ 1,449,866	$ 214,655	$ 12,712,395
onimpaired ans/leases	1,271,448,649	1,342,351,489	130,667,609	255,983,847	92,737,469	3,093,189,063
	$ 1,273,000,094	$ 1,349,318,914	$ 133,196,613	$ 257,433,713	$ 92,952,124	$ 3,105,901,458
lowance a rcentage impaired ans/leases	19.86 %	30.27 %	14.86 %	16.51 %	49.79 %	24.70
lowance a rcentage nimpaired ans/leases	1.17 %	1.02 %	1.80 %	0.86 %	1.32 %	1.11
tal owance as percentage total ans/leases	1.20 %	1.17 %	2.05 %	0.95 %	1.44 %	1.21

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	As of December 31, 2017					
	C&I	CRE	Direct Financing Leases	Residential Real Estate	Installment and Other Consumer	Total
owance impaired ns/leases	$ 715,627	$ 1,429,460	$ 504,469	$ 355,167	$ 38,596	$ 3,043,319
owance nimpaired ns/leases	13,607,409	12,533,228	1,877,629	2,111,264	1,182,879	31,312,409
	$ 14,323,036	$ 13,962,688	$ 2,382,098	$ 2,466,431	$ 1,221,475	$ 34,355,728
paired ns/leases	$ 6,248,209	$ 6,529,262	$ 3,669,492	$ 1,704,846	$ 202,354	$ 18,354,163
nimpaired ns/leases	1,128,268,106	1,296,962,620	137,778,740	256,941,419	118,408,445	2,938,359,330
	$ 1,134,516,315	$ 1,303,491,882	$ 141,448,232	$ 258,646,265	$ 118,610,799	$ 2,956,713,493
owance a centage mpaired ns/leases	11.45 %	21.89 %	13.75 %	20.83 %	19.07 %	16.58
owance a centage nimpaired ns/leases	1.21 %	0.97 %	1.36 %	0.82 %	1.00 %	1.07
al owance as ercentage otal ns/leases	1.26 %	1.07 %	1.68 %	0.95 %	1.03 %	1.16

Information for impaired loans/leases is presented in the tables below. The recorded investment represents customer balances net of any partial charge-offs recognized on the loan/lease. The unpaid principal balance represents the recorded balance outstanding on the loan/lease prior to any partial charge-offs.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - continued

Loans/leases, by classes of financing receivable, considered to be impaired as of and for the six months ended June 30, 2018 are presented as follows:

Classes of Loans/Leases	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized	Interest Income Recognized for Cash Payments Received
Impaired Loans/Leases with No Specific Allowance Recorded:						
C&I	$ 1,159,577	$ 1,173,853	$ —	$ 1,465,402	$ 138,543	$ 138,543
CRE Owner-Occupied CRE	288,813	288,813	—	289,112	11,690	11,690
Commercial Construction, Land Development, and Other Land	—	—	—	—	—	—
Other Non Owner-Occupied CRE	982,428	982,428	—	1,151,245	—	—
Direct Financing Leases	1,903,173	1,903,173	—	2,551,149	9,292	9,292
Residential Real Estate	941,520	1,016,299	—	904,898	—	—
Installment and Other Consumer	99,814	99,814	—	95,448	—	—
	$ 5,375,325	$ 5,464,380	$ —	$ 6,457,254	$ 159,525	$ 159,525
Impaired Loans/Leases with Specific Allowance Recorded:						
C&I	$ 391,868	$ 391,868	$ 308,091	$ 327,859	$ —	$ —
CRE						
	142,788	142,788	39,288	147,375	—	—

Owner-Occupied CRE						
Commercial Construction, Land Development, and Other Land	5,553,396	5,553,396	2,070,086	5,275,992	—	—
Other Non Owner-Occupied CRE	—	—	—	—	—	—
Direct Financing Leases	625,831	625,831	375,803	521,142	—	—
Residential Real Estate	508,346	531,422	239,419	522,134	5,893	5,893
Installment and Other Consumer	114,841	114,841	106,878	109,254	159	159
	$ 7,337,070	$ 7,360,146	$ 3,139,565	$ 6,903,756	$ 6,052	$ 6,052
Total Impaired Loans/Leases:						
C&I	$ 1,551,445	$ 1,565,721	$ 308,091	$ 1,793,261	$ 138,543	$ 138,543
CRE Owner-Occupied CRE	431,601	431,601	39,288	436,487	11,690	11,690
Commercial Construction, Land Development, and Other Land	5,553,396	5,553,396	2,070,086	5,275,992	—	—
Other Non Owner-Occupied CRE	982,428	982,428	—	1,151,245	—	—
Direct Financing Leases	2,529,004	2,529,004	375,803	3,072,291	9,292	9,292
Residential Real Estate	1,449,866	1,547,721	239,419	1,427,032	5,893	5,893
Installment and Other Consumer	214,655	214,655	106,878	204,702	159	159
	$ 12,712,395	$ 12,824,526	$ 3,139,565	$ 13,361,010	$ 165,577	$ 165,577

Impaired loans/leases for which no allowance has been provided have adequate collateral, based on management's current estimates.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - continued

Loans/leases, by classes of financing receivable, considered to be impaired as of and for the three months ended June 30, 2018 and 2017, respectively, are presented as follows:

	Three Months Ended June 30, 2018			Three Months Ended June 30, 2017		
Classes of Loans/Leases	Average Recorded Investment	Interest Income Recognized	Interest Income Recognized for Cash Payments Received	Average Recorded Investment	Interest Income Recognized	Interest Income Recognized for Cash Payments Received
Impaired Loans/Leases with No Specific Allowance Recorded:						
C&I	$ 1,400,498	$ 59,176	$ 59,176	$ 805,309	$ 9,399	$ 9,399
CRE Owner-Occupied CRE	289,036	5,868	5,868	—	—	—
Commercial Construction, Land Development, and Other Land	—	—	—	—	—	—
Other Non Owner-Occupied CRE	1,105,004	—	—	1,160,161	—	—
Direct Financing Leases	2,198,852	2,544	2,544	2,560,019	38,949	38,949
Residential Real Estate	928,809	—	—	712,793	—	—
Installment and Other Consumer	101,582	—	—	173,585	218	218
	$ 6,023,781	$ 67,588	$ 67,588	$ 5,411,867	$ 48,566	$ 48,566
Impaired Loans/Leases with Specific Allowance Recorded:						
C&I	$ 353,153	$ 1,978	$ 1,978	$ 8,066,702	$ 35,055	$ 35,055
CRE Owner-Occupied CRE	145,082	—	—	238,584	—	—

Commercial Construction, Land Development, and Other Land	5,491,832	—	—	4,348,142	—	—
Other Non Owner-Occupied CRE	—	—	—	38,260	—	—
Direct Financing Leases	566,063	—	—	757,602	—	—
Residential Real Estate	512,222	2,959	2,959	624,641	2,989	2,989
Installment and Other Consumer	116,887	76	76	34,333	—	—
	$ 7,185,239	$ 5,014	$ 5,014	$ 14,108,264	$ 38,044	$ 38,044
Total Impaired Loans/Leases:						
C&I	$ 1,753,651	$ 61,154	$ 61,154	$ 8,872,011	$ 44,454	$ 44,454
CRE Owner-Occupied CRE	434,118	5,868	5,868	238,584	—	—
Commercial Construction, Land Development, and Other Land	5,491,832	—	—	4,348,142	—	—
Other Non Owner-Occupied CRE	1,105,004	—	—	1,198,421	—	—
Direct Financing Leases	2,764,915	2,544	2,544	3,317,621	38,949	38,949
Residential Real Estate	1,441,031	2,959	2,959	1,337,434	2,989	2,989
Installment and Other Consumer	218,469	76	76	207,918	218	218
	$ 13,209,020	$ 72,602	$ 72,602	$ 19,520,131	$ 86,610	$ 86,610

Impaired loans/leases for which no allowance has been provided have adequate collateral, based on management's current estimates.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - continued

Loans/leases, by classes of financing receivable, considered to be impaired as of December 31, 2017 are presented as follows:

Classes of Loans/Leases	Recorded Investment	Unpaid Principal Balance	Related Allowance
Impaired Loans/Leases with No Specific Allowance Recorded:			
C&I	$ 1,634,269	$ 1,644,706	$ —
CRE			
Owner-Occupied CRE	289,261	289,261	—
Commercial Construction, Land Development, and Other Land	—	—	—
Other Non Owner-Occupied CRE	1,171,565	1,171,565	—
Direct Financing Leases	2,944,540	2,944,540	—
Residential Real Estate	943,388	1,018,167	—
Installment and Other Consumer	134,245	134,245	—
	$ 7,117,268	$ 7,202,484	$ —
Impaired Loans/Leases with Specific Allowance Recorded:			
C&I	$ 4,613,940	$ 4,617,879	$ 715,627
CRE			
Owner-Occupied CRE	151,962	151,962	48,462
Commercial Construction, Land Development, and Other Land	4,844,312	4,844,312	1,379,235
Other Non Owner-Occupied CRE	72,163	72,163	1,763
Direct Financing Leases	724,953	724,953	504,469
Residential Real Estate	761,458	761,458	355,167
Installment and Other Consumer	68,109	68,109	38,596
	$ 11,236,897	$ 11,240,836	$ 3,043,319
Total Impaired Loans/Leases:			
C&I	$ 6,248,209	$ 6,262,585	$ 715,627
CRE			
Owner-Occupied CRE	441,222	441,222	48,462
Commercial Construction, Land Development, and Other Land	4,844,312	4,844,312	1,379,235
Other Non Owner-Occupied CRE	1,243,728	1,243,728	1,763
Direct Financing Leases	3,669,492	3,669,492	504,469
Residential Real Estate	1,704,846	1,779,625	355,167
Installment and Other Consumer	202,354	202,354	38,596

$ 18,354,163	$ 18,443,318	$ 3,043,319

Impaired loans/leases for which no allowance has been provided have adequate collateral, based on management's current estimates.

For C&I and CRE loans, the Company's credit quality indicator consists of internally assigned risk ratings. Each commercial loan is assigned a risk rating upon origination. The risk rating is reviewed every 15 months, at a minimum, and on an as-needed basis depending on the specific circumstances of the loan.

For certain C&I loans (equipment financing agreements), direct financing leases, residential real estate loans, and installment and other consumer loans, the Company's credit quality indicator is performance determined by delinquency status. Delinquency status is updated daily by the Company's loan system.

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For each class of financing receivable, the following presents the recorded investment by credit quality indicator as of June 30, 2018 and December 31, 2017:

As of June 30, 2018		CRE				
		Owner-Occupied	Non Owner-Occupied Commercial Construction, Land Development,			As a % of
Internally Assigned Risk Rating	C&I	CRE	and Other Land	Other CRE	Total	Total
Pass (Ratings 1 through 5)	$ 1,135,035,263	$ 342,518,625	$ 160,224,065	$ 805,031,050	$ 2,442,809,003	96.57 %
Special Mention (Rating 6)	29,414,324	3,984,113	—	10,804,187	44,202,624	1.75 %
Substandard (Rating 7)	15,734,765	2,505,092	2,420,501	21,831,281	42,491,639	1.68 %
Doubtful (Rating 8)	—	—	—	—	—	— %
	$ 1,180,184,352	$ 349,007,830	$ 162,644,566	$ 837,666,518	$ 2,529,503,266	100.00 %

As of June 30, 2018		Direct Financing	Residential Real	Installment and		As a % of
Delinquency Status *	C&I	Leases	Estate	Other Consumer	Total	Total
Performing	$ 92,361,366	$ 130,530,177	$ 255,847,659	$ 92,718,538	$ 571,457,740	99.14 %
Nonperforming	454,376	2,666,436	1,586,054	233,586	4,940,452	0.86 %
	$ 92,815,742	$ 133,196,613	$ 257,433,713	$ 92,952,124	$ 576,398,192	100.00 %

As of December 31, 2017

CRE

Non Owner-Occupied

Internally Assigned Risk Rating	C&I	Owner-Occupied CRE	Commercial Construction, Land Development, and Other Land	Other CRE	Total	As a % of Total	
Pass (Ratings 1 through 5)	$ 1,031,963,703	$ 318,293,608	$ 179,142,839	$ 767,119,909	$ 2,296,520,059	96.85	%
Special Mention (Rating 6)	10,944,924	8,230,060	1,780,000	10,068,870	31,023,854	1.31	%
Substandard (Rating 7)	24,578,731	6,218,809	5,479,565	7,158,221	43,435,326	1.83	%
Doubtful (Rating 8)	270,559	—	—	—	270,559	0.01	%
	$ 1,067,757,917	$ 332,742,477	$ 186,402,404	$ 784,347,000	$ 2,371,249,799	100.00	%

	As of December 31, 2017						
Delinquency Status *	C&I	Direct Financing Leases	Residential Real Estate	Installment and Other Consumer	Total	As a % of Total	
Performing	$ 65,847,177	$ 137,778,740	$ 256,935,447	$ 118,333,529	$ 578,894,893	98.88	%
Nonperforming	911,220	3,669,492	1,710,818	277,270	6,568,800	1.12	%
	$ 66,758,397	$ 141,448,232	$ 258,646,265	$ 118,610,799	$ 585,463,693	100.00	%

* Performing = loans/leases accruing and less than 90 days past due. Nonperforming = loans/leases on nonaccrual, accruing loans/leases that are greater than or equal to 90 days past due, and accruing TDRs.

As of June 30, 2018 and December 31, 2017, TDRs totaled $3,168,014 and $9,394,967, respectively.

For each class of financing receivable, the following presents the number and recorded investment of TDRs, by type of concession, that were restructured during the three and six months ended June 30, 2018 and 2017. The difference between

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the pre-modification recorded investment and the post-modification recorded investment would be any partial charge-offs at the time of the restructuring. No loans were restructured during the three months ended June 30, 2018.

	For the three months ended June 30, 2018				For the three months ended June 30, 2017			
Classes of Loans/Leases	Number of Loans / Leases	Pre-Modification Recorded Investment	Post-Modification Recorded Investment	Specific Allowance	Number of Loans / Leases	Pre-Modification Recorded Investment	Post-Modification Recorded Investment	Specific Allowanc
CONCESSION - Significant Payment Delay								
C&I	—	$ —	$ —	$ —	1	$ 47,509	$ 47,509	$ —
Direct Financing Leases	—	—	—	—	15	802,542	802,542	—
	—	$ —	$ —	$ —	16	$ 850,051	$ 850,051	$ —
CONCESSION - Extension of Maturity								
Direct Financing Leases	—	$ —	$ —	$ —	1	$ 98,119	$ 98,119	$ —
	—	$ —	$ —	$ —	1	$ 98,119	$ 98,119	$ —
TOTAL	—	$ —	$ —	$ —	17	$ 948,170	$ 948,170	$ —

	For the six months ended June 30, 2018				For the six months ended June 30, 2017			
Classes of Loans/Leases	Number of Loans/Leases	Pre-Modification Recorded Investment	Post-Modification Recorded Investment	Specific Allowance	Number of Loans/Leases	Pre-Modification Recorded Investment	Post-Modification Recorded Investment	Spec Allo
CONCESSION - Extension of Maturity								
Direct Financing Leases	—	—	—	—	2	104,382	104,382	–
	—	$ —	$ —	$ —	2	$ 104,382	$ 104,382	$ –

CONCESSION - Significant Payment Delay								
C&I	—	$ —	$ —	$ —	3	$ 181,198	$ 181,198	$ –
Real Estate	1	46,320	46,320	—	—	—	—	
Direct Financing Leases	2	47,524	47,524	—	23	1,472,403	1,472,403	–
	3	$ 93,844	$ 93,844	$ —	26	$ 1,653,601	$ 1,653,601	$ –
TOTAL	3	$ 93,844	$ 93,844	$ —	28	$ 1,757,983	$ 1,757,983	$ –

Of the TDRs reported above, one with a post-modification recorded balance of $46,320 was on nonaccrual as of June 30, 2018. Of the TDRs reported above, none were on nonaccrual as of June 30, 2017.

For the three and six months ended June 30, 2018, seven of the Company's TDRs redefaulted within 12 months subsequent to restructure where default is defined as delinquency of 90 days or more and/or placement on nonaccrual status. Three of these TDRs were related to one customer whose loans were restructured in the second quarter of 2017 with pre-modification balances totaling $78 thousand and the other TDRs related to other customers whose loans were restructured in the second and third quarters of 2017 with pre-modification balances totaling $378 thousand.

For the three and six months ended June 30, 2017, two of the Company's TDRs redefaulted within 12 months subsequent to restructure where default is defined as delinquency of 90 days or more and/or placement on nonaccrual status. These two TDRs were related to the same customer and were restructured in the fourth quarter of 2016 with pre-modification balances totaling $195 thousand.

Not included in the table above, the Company had 8 TDRs that were restructured and charged off in 2018, totaling $577,377. The Company had 2 TDRs that were restructured and charged off in 2017, totaling $65,623.

NOTE 4 – DERIVATIVES

The Company uses interest rate swap and cap instruments to manage interest rate risk related to the variability of interest payments due to changes in interest rates. The Company entered into interest rate caps on June 5, 2014 to hedge against the risk of rising interest rates on short-term liabilities. The short-term liabilities consist of $30.0 million of 1-month FHLB advances, and the benchmark rate hedged is 1-month LIBOR. The interest rate caps are designated as a cash flow

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hedge in accordance with ASC 815. An initial premium of $2.1 million was paid upfront for the two caps. The details of the interest rate caps are as follows:

Hedged Instrument	Effective Date	Maturity Date	Balance Sheet Location	Notional Amount	1-Month LIBOR Strike Rate	Fair Value as of June 30, 2018	Fair Value as of December 31, 2017
1-month FHLB Advance	6/3/2014	6/5/2019	Other Assets	$ 15,000,000	1.00%	$ 199,821	$ 190,085
1-month FHLB Advance	6/5/2014	6/5/2021	Other Assets	15,000,000	1.50%	506,470	316,615
				$ 30,000,000		$ 706,291	$ 506,700

On June 21, 2018, the Company entered into interest rate swaps to hedge against the risk of rising rates on its variable rate trust preferred securities. The floating rate trust preferred securities are tied to 3-month LIBOR, and the interest rate swaps utilize 3-month LIBOR, so the hedge is effective. The interest rate swaps are designated as a cash flow hedge in accordance with ASC 815. The details of the interest rate swaps are as follows:

Hedged Instrument	Effective Date	Maturity Date	Balance Sheet Location	Notional Amount	Receive Rate	Pay Rate	Fair Value as of June 30, 2018
QCR Holdings Statutory Trust II	9/30/2018	9/30/2028	Other Liabilities	$ 10,000,000	5.19%	5.85%	$ (94,210)
QCR Holdings Statutory Trust III	9/30/2018	9/30/2028	Other Liabilities	8,000,000	5.19%	5.85%	(75,368)
QCR Holdings Statutory Trust V	7/7/2018	7/7/2028	Other Liabilities	10,000,000	3.90%	4.54%	(97,961)
Community National Statutory Trust II	9/20/2018	9/20/2028	Other Liabilities	3,000,000	4.49%	5.17%	(28,329)
Community National Statutory Trust III	9/15//2018	9/15/2028	Other Liabilities	3,500,000	4.09%	4.75%	(33,330)
Guaranty Bankshares	9/15/2018	9/15/2028	Other Liabilities	4,500,000	4.09%	4.75%	(42,852)

Statutory Trust I	$ 39,000,000	4.58%	5.24%	$ (372,050)

Changes in fair values of derivatives designated as cash flow hedges are recorded in OCI to the extent the hedge is effective, and reclassified to earnings as the hedged transaction (interest payments on debt) impact earnings.

The caps and swaps are valued by the transaction counterparty on a monthly basis and corroborated by a third party annually.

NOTE 5 - EARNINGS PER SHARE

The following information was used in the computation of EPS on a basic and diluted basis:

	Three months ended June 30,		Six months ended June 30,	
	2018	2017	2018	2017
Net income	$ 10,445,385	$ 8,766,017	$ 20,995,346	$ 17,950,982
Basic EPS	$ 0.75	$ 0.67	$ 1.51	$ 1.36
Diluted EPS	$ 0.73	$ 0.65	$ 1.48	$ 1.33
Weighted average common shares outstanding	13,919,565	13,170,283	13,904,113	13,151,833
Weighted average common shares issuable upon exercise of stock options and under the employee stock purchase plan	312,858	346,309	314,890	350,672
Weighted average common and common equivalent shares outstanding	14,232,423	13,516,592	14,219,003	13,502,505

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The increase in weighted average common shares outstanding when comparing the three and six months ended June 30, 2018 to June 30, 2017 was primarily due to the common stock issuance discussed in Note 2 to the Consolidated Financial Statements included in the Company's Annual Report on Form 10 K for the year ended December 31, 2017.

NOTE 6 – FAIR VALUE

Accounting guidance on fair value measurement uses a hierarchy intended to maximize the use of observable inputs and minimize the use of unobservable inputs. This hierarchy includes three levels and is based upon the valuation techniques used to measure assets and liabilities. The three levels are as follows:

- Level 1 – Inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in markets;
- Level 2 – Inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument; and
- Level 3 – Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

Assets and liabilities measured at fair value on a recurring basis comprise the following at June 30, 2018 and December 31, 2017:

		Fair Value Measurements at Reporting Date Using		
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
June 30, 2018:				
Securities AFS:				
U.S. govt. sponsored agency securities	$ 35,666,536	$ —	$ 35,666,536	$ —
Residential mortgage-backed and related securities	158,534,448	—	158,534,448	—
Municipal securities	59,507,267	—	59,507,267	—
Other securities	4,236,420	—	4,236,420	—
Interest rate caps	706,291	—	706,291	—
Interest rate swaps - assets	6,171,740	—	6,171,740	
Total assets measured at fair value	$ 264,822,702	$ —	$ 264,822,702	$ —
Interest rate swaps - liabilities	$ 6,543,790	$ —	$ 6,543,790	$ —
Total liabilities measured at fair value	$ 6,543,790	$ —	$ 6,543,790	$ —

December 31, 2017:				
Securities AFS:				
U.S. govt. sponsored agency securities	$ 38,096,534	$ —	$ 38,096,534	$ —
Residential mortgage-backed and related securities	163,301,304	—	163,301,304	—
Municipal securities	66,625,496	—	66,625,496	—
Other securities	4,884,573	1,028	4,883,545	—
Interest rate caps	506,700	—	506,700	—
Interest rate swaps - assets	4,397,238	—	4,397,238	
Total assets measured at fair value	$ 277,811,845	$ 1,028	$ 277,810,817	$ —
Interest rate swaps - liabilities	$ 4,397,238	$ —	$ 4,397,238	$ —
Total liabilities measured at fair value	$ 4,397,238	$ —	$ 4,397,238	$ —

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There were no transfers of assets or liabilities between Levels 1, 2, and 3 of the fair value hierarchy for the three and six months ended June 30, 2018 or 2017.

The securities AFS portfolio consists of securities whereby the Company obtains fair values from an independent pricing service. The fair values are determined by pricing models that consider observable market data, such as interest rate volatilities, LIBOR yield curve, credit spreads and prices from market makers and live trading systems (Level 2 inputs).

Interest rate caps are used for the purpose of hedging interest rate risk. The fair values are determined by pricing models that consider observable market data for derivative instruments with similar structures (Level 2 inputs).

Interest rate swaps are executed for select commercial customers. The interest rate swaps are further described in Note 1 to the Consolidated Financial Statements included in the Company's Annual Report on Form 10 K for the year ended December 31, 2017. The fair values are determined by comparing the contract rate on the swap with the then-current market rate for the remaining term of the transaction (Level 2 inputs).

Interest rate swaps are also used for the purpose of hedging interest rate risk on junior subordinated debt. The fair values are determined by comparing the contract rate on the swap with the then-current market rate for the remaining term of the transaction (Level 2 inputs).

Certain financial assets are measured at fair value on a non-recurring basis; that is, the assets are not measured at fair value on an ongoing basis but are subject to fair value adjustments in certain circumstances (for example, when there is evidence of impairment).

Assets measured at fair value on a non-recurring basis comprise the following at June 30, 2018 and December 31, 2017:

		Fair Value Measurements at Reporting Date Using		
	Fair Value	Quoted Prices in Active Markets for Identical Assets Level 1	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3
June 30, 2018:				
Impaired loans/leases	$ 4,674,218	$ —	$ —	$ 4,674,218
OREO	13,770,025	—	—	13,770,025
	$ 18,444,243	$ —	$ —	$ 18,444,243
December 31, 2017:				
Impaired loans/leases	$ 8,972,337	$ —	$ —	$ 8,972,337
OREO	14,642,973	—	—	14,642,973
	$ 23,615,310	$ —	$ —	$ 23,615,310

Impaired loans/leases are evaluated and valued at the time the loan/lease is identified as impaired, at the lower of cost or fair value, and are classified as Level 3 in the fair value hierarchy. Fair value is measured based on the value of the collateral securing these loans/leases. Collateral may be real estate and/or business assets, including equipment, inventory and/or accounts receivable, and is determined based on appraisals by qualified licensed appraisers hired by the Company. Appraised and reported values are discounted based on management's historical knowledge, changes in market conditions from the time of valuation, and/or management's expertise and knowledge of the client and client's business.

OREO in the table above consists of property acquired through foreclosures and settlements of loans. Property acquired is carried at the estimated fair value of the property, less disposal costs, and is classified as Level 3 in the fair value hierarchy.

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The estimated fair value of the property is determined based on appraisals by qualified licensed appraisers hired by the Company. Appraised and reported values are discounted based on management's historical knowledge, changes in market conditions from the time of valuation, and/or management's expertise and knowledge of the property.

The following table presents additional quantitative information about assets measured at fair value on a non-recurring basis for which the Company has utilized Level 3 inputs to determine fair value:

	Quantitative Information about Level Fair Value Measurements						
	Fair Value June 30, 2018	Fair Value December 31, 2017	Valuation Technique	Unobservable Input	Range		
Impaired loans/leases	$ 4,674,218	$ 8,972,337	Appraisal of collateral	Appraisal adjustments	(10.00)%	to	(30.00)%
OREO	13,770,025	14,642,973	Appraisal of collateral	Appraisal adjustments	0.00 %	to	(35.00)%

For the impaired loans/leases and OREO, the Company records carrying value at fair value less disposal or selling costs. The amounts reported in the tables above are fair values before the adjustment for disposal or selling costs.

There have been no changes in valuation techniques used for any assets measured at fair value during the three and six months ended June 30, 2018 and 2017.

The following table presents the carrying values and estimated fair values of financial assets and liabilities carried on the Company's consolidated balance sheets, including those financial assets and liabilities that are not measured and reported at fair value on a recurring basis or non-recurring basis:

	Fair Value Hierarchy Level	As of June 30, 2018		As of December 31, 2017	
		Carrying Value	Estimated Fair Value	Carrying Value	Estimated Fair Value
Cash and due from banks	Level 1	$ 69,069,403	$ 69,069,403	$ 75,721,663	$ 75,721,663
Federal funds sold	Level 2	10,866,000	10,866,000	30,197,000	30,197,000
Interest-bearing deposits at financial institutions	Level 2	40,801,388	40,801,388	55,765,012	55,765,012
Investment securities:					
HTM	Level 2	400,052,344	397,252,368	379,474,205	379,749,804

AFS	See Previous Table	257,944,671	257,944,671	272,907,907	272,907,907
Loans/leases receivable, net	Level 3	4,327,980	4,674,218	8,307,719	8,972,337
Loans/leases receivable, net	Level 2	3,072,919,367	3,020,805,000	2,921,821,953	2,892,963,000
Interest rate caps	Level 2	706,291	706,291	506,700	506,700
Interest rate swaps - assets	Level 2	6,171,740	6,171,740	4,397,238	4,397,238
Deposits:					
Nonmaturity deposits	Level 2	2,622,243,626	2,622,243,626	2,670,583,178	2,670,583,178
Time deposits	Level 2	676,032,401	677,799,000	596,071,878	591,772,000
Short-term borrowings	Level 2	17,585,605	17,585,605	13,993,122	13,993,122
FHLB advances	Level 2	254,100,000	254,008,000	192,000,000	192,115,000
Other borrowings	Level 2	71,125,000	71,645,000	66,000,000	66,520,000
Junior subordinated debentures	Level 2	37,580,881	29,851,237	37,486,487	29,253,624
Interest rate swaps - liabilities	Level 2	6,543,790	6,543,790	4,397,238	4,397,238

NOTE 7 – BUSINESS SEGMENT INFORMATION

Selected financial and descriptive information is required to be disclosed for reportable operating segments, applying a “management perspective” as the basis for identifying reportable segments. The management perspective is determined by the view that management takes of the segments within the Company when making operating decisions, allocating resources, and measuring performance. The segments of the Company have been defined by the structure of the Company's internal organization, focusing on the financial information that the Company's operating decision-makers routinely use to make decisions about operating matters.

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The Company's primary segment, Commercial Banking, is geographically divided by markets into the secondary segments comprised of the five subsidiary banks wholly owned by the Company: QCBT, CRBT, CSB, RB&T and SFC Bank. Each of these secondary segments offers similar products and services, but is managed separately due to different pricing, product demand, and consumer markets. Each offers commercial, consumer, and mortgage loans and deposit services.

The Company's Wealth Management segment represents the trust and asset management and investment management and advisory services offered at the Company's five subsidiary banks in aggregate. This segment generates income primarily from fees charged based on assets under administration for corporate and personal trusts, custodial services, and investments managed. No assets of the subsidiary banks have been allocated to the Wealth Management segment.

The Company's All Other segment includes the operations of all other consolidated subsidiaries and/or defined operating segments that fall below the segment reporting thresholds. This segment includes the corporate operations of the parent company.

Selected financial information on the Company's business segments is presented as follows as of and for the three and six months ended June 30, 2018 and 2017.

Commercial Banking				Wealth		Intercompany
QCBT	CRBT	CSB	RB&T	Management	All other	Eliminations
$ 16,682,874	$ 16,503,977	$ 8,406,295	$ 5,119,916	$ 3,115,653	$ 13,024,443	$ (13,142,678)
12,290,034	10,481,055	6,734,510	3,401,849	—	(822,952)	—
1,254,493	627,742	221,000	197,500	—	—	—
4,510,902	4,705,042	2,158,347	813,623	796,911	10,405,693	(12,945,133)
3,222,688	14,979,984	9,888,225	—	—	—	—
—	3,439,864	5,029,987	—	—	—	—
1,563,643,434	1,345,431,093	712,138,515	484,123,277	—	463,206,792	(461,660,406)
$ 14,210,040	$ 10,149,769	$ 8,171,307	$ 4,241,431	$ 2,560,836	$ 10,181,814	$ (10,279,411)
11,414,818	7,230,425	6,920,820	3,095,512	—	(614,878)	—
552,993	300,000	861,000	309,000	—	—	—
4,073,777	2,870,582	1,920,040	834,842	454,465	8,766,014	(10,153,703)
3,222,688	—	9,888,225	—	—	—	—

—	1,172,141	5,747,339	—	—	—	—
1,400,307,827	993,768,912	642,761,140	426,159,677	—	382,407,292	(388,218,153)
$ 32,490,444	$ 32,501,309	$ 16,569,618	$ 10,117,861	$ 6,305,078	$ 25,556,486	$ (25,742,571)
24,410,336	21,316,903	13,478,457	6,867,003	—	(1,585,285)	—
2,374,902	1,229,570	796,602	439,500	—	—	—
8,968,770	9,321,570	4,026,935	1,554,918	1,567,776	20,920,203	(25,364,826)
3,222,688	14,979,984	9,888,225	—	—	—	—
—	3,439,864	5,029,987	—	—	—	—
1,563,643,434	1,345,431,093	712,138,515	484,123,277	—	463,206,792	(461,660,406)
$ 27,745,981	$ 20,536,314	$ 16,303,013	$ 8,189,230	$ 5,262,642	$ 20,057,957	$ (20,230,498)
22,716,300	14,204,472	13,947,328	6,063,586	—	(1,216,106)	—
1,484,102	550,000	1,635,000	459,000	—	—	—
7,728,783	5,763,142	3,815,174	1,679,411	1,015,527	17,950,982	(20,002,037)
3,222,688	—	9,888,225	—	—	—	—
—	1,172,141	5,747,339	—	—	—	—
1,400,307,827	993,768,912	642,761,140	426,159,677	—	382,407,292	(388,218,153)

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NOTE 8 – REGULATORY CAPITAL REQUIREMENTS

The Company (on a consolidated basis) and the subsidiary banks are subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Company and subsidiary banks' financial statements.

Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company and the subsidiary banks must meet specific capital guidelines that involve quantitative measures of their assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices. The capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors. Quantitative measures established by regulation to ensure capital adequacy require the Company and the subsidiary banks to maintain minimum amounts and ratios (set forth in the following table) of total common equity Tier 1 and Tier 1 capital to risk-weighted assets and of Tier 1 capital to average assets, each as defined by regulation. Management believes, as of June 30, 2018 and December 31, 2017, that the Company and the subsidiary banks met all capital adequacy requirements to which they are subject.

Under the regulatory framework for prompt corrective action, to be categorized as “well capitalized,” an institution must maintain minimum total risk-based, Tier 1 risk-based, Tier 1 leverage and common equity Tier 1 ratios as set forth in the following tables. The Company and the subsidiary banks' actual capital amounts and ratios as of June 30, 2018 and December 31, 2017 are presented in the following table (dollars in thousands). As of June 30, 2018 and December 31, 2017, each of the subsidiary banks met the requirements to be “well capitalized”.

	Actual Amount	Ratio	For Capital Adequacy Purposes Amount	Ratio	For Capital Adequacy Purposes With Capital Conservation Buffer* Amount	Ratio	To Be Well Capitalized Under Prompt Corrective Action Provisions Amount	Ratio
of e 30, 2018:								
mpany:								
tal k-based pital	$ 407,222	11.23 %	$ 290,121	> 8.00 %	$ 358,118	> 9.875 %	$ 362,652	> 10.00
r 1 k-based pital	369,677	10.19 %	217,591	> 6.00	285,588	> 7.875	290,121	> 8.00
r 1 leverage	369,677	9.22 %	160,373	> 4.00	160,373	> 4.000	200,466	> 5.00
mmon ity Tier 1	332,096	9.16 %	163,193	> 4.50	231,190	> 6.375	235,723	> 6.50
ad City nk & Trust:								

tal k-based bital	$ 158,480	11.67 %	$ 108,599	>	8.00	%	$ 134,052	>	9.875 %	$ 135,748	>	10.00
r 1 k-based bital	145,157	10.69 %	81,449	>	6.00		106,902	>	7.875	108,599	>	8.00
r 1 leverage	145,157	9.19 %	63,193	>	4.00		63,193	>	4.000	78,992	>	5.00
mmon uity Tier 1	145,157	10.69 %	61,087	>	4.50		86,540	>	6.375	88,236	>	6.50
dar Rapids nk & Trust:												
tal k-based bital	$ 143,414	11.76 %	$ 97,602	>	8.00	%	$ 120,477	>	9.875 %	$ 122,003	>	10.00
r 1 k-based bital	130,203	10.67 %	73,202	>	6.00		96,077	>	7.875	97,602	>	8.00
r 1 leverage	130,203	9.83 %	52,961	>	4.00		52,961	>	4.000	66,201	>	5.00
mmon uity Tier 1	130,203	10.67 %	54,901	>	4.50		77,777	>	6.375	79,302	>	6.50
mmunity te Bank:												
tal k-based bital	$ 70,656	11.70 %	$ 48,330	>	8.00	%	$ 59,658	>	9.875 %	$ 60,413	>	10.00
r 1 k-based bital	65,443	10.83 %	36,248	>	6.00		47,575	>	7.875	48,330	>	8.00
r 1 leverage	65,443	9.56 %	27,384	>	4.00		27,384	>	4.000	34,229	>	5.00
mmon uity Tier 1	65,443	10.83 %	27,186	>	4.50		38,513	>	6.375	39,268	>	6.50
ckford Bank Trust:												
tal k-based bital	$ 47,697	10.81 %	$ 35,283	>	8.00	%	$ 43,553	>	9.875 %	$ 44,104	>	10.00
r 1 k-based bital	42,181	9.56 %	26,463	>	6.00		34,732	>	7.875	35,283	>	8.00
r 1 leverage	42,181	8.90 %	18,947	>	4.00		18,947	>	4.000	23,684	>	5.00
mmon uity Tier 1	42,181	9.56 %	19,847	>	4.50		28,116	>	6.375	28,668	>	6.50

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	Actual Amount	Ratio		For Capital Adequacy Purposes Amount		Ratio		For Capital Adequacy Purposes With Capital Conservation Buffer* Amount		Ratio		To Be Well Capitalized Under Prompt Corrective Action Provisions Amount		Rat
mber 31, 2017:														
any:														
risk-based														
l	$ 383,282	11.15	%	$ 275,090	>	8.00	%	$ 318,073	>	9.25	%	$ 343,862	>	10.0
risk-based														
l	348,530	10.14	%	206,317	>	6.00		249,300	>	7.25		275,090	>	8.00
leverage	348,530	8.98	%	155,256	>	4.00		155,256	>	4.00		194,070	>	5.00
non equity Tier														
	313,012	9.10	%	154,738	>	4.50		197,721	>	5.75		223,510	>	6.50
City Bank &														
risk-based														
l	$ 160,112	12.35	%	$ 103,711	>	8.00	%	$ 119,916	>	9.25	%	$ 129,639	>	10.0
risk-based														
l	147,472	11.38	%	77,783	>	6.00		93,988	>	7.25		103,711	>	8.00
leverage	147,472	9.52	%	61,985	>	4.00		61,985	>	4.00		77,481	>	5.00
non equity Tier														
	147,472	11.38	%	58,337	>	4.50		74,542	>	5.75		84,265	>	6.50
Rapids Bank														
st:														
risk-based														
l	$ 138,492	11.88	%	$ 93,272	>	8.00	%	$ 107,846	>	9.25	%	$ 116,590	>	10.0
risk-based														
l	126,601	10.86	%	69,954	>	6.00		84,528	>	7.25		93,272	>	8.00
leverage	126,601	11.68	%	43,348	>	4.00		43,348	>	4.00		54,185	>	5.00
non equity Tier														
	126,601	10.86	%	52,465	>	4.50		67,039	>	5.75		75,783	>	6.50
nunity State														
risk-based														
l	$ 66,271	11.71	%	$ 45,293	>	8.00	%	$ 52,370	>	9.25	%	$ 56,616	>	10.0
risk-based														
l	61,941	10.94	%	33,970	>	6.00		41,047	>	7.25		45,293	>	8.00
leverage	61,941	9.77	%	25,354	>	4.00		25,354	>	4.00		31,693	>	5.00
	61,941	10.94	%	25,477	>	4.50		32,554	>	5.75		36,801	>	6.50

non equity Tier											
ford Bank &											
risk-based l	$ 45,684	11.28 %	$ 32,413	>	8.00 %	$ 37,477	>	9.25 %	$ 40,516	>	10.0
risk-based l	40,615	10.02 %	24,310	>	6.00	29,374	>	7.25	32,413	>	8.0
leverage	40,615	8.94 %	18,177	>	4.00	18,177	>	4.00	22,721	>	5.0
non equity Tier	40,615	10.02 %	18,232	>	4.50	23,297	>	5.75	26,335	>	6.5

* The minimums under Basel III increase by .625% (the capital conservation buffer) annually until 2019. The fully phased-in minimums are 10.5% (Total risk-based capital), 8.5% (Tier 1 risk-based capital), and 7.0% (Common equity Tier 1).

NOTE 9 – REVENUE RECOGNITION

As of January 1, 2018, the Company adopted ASU 2014 09 using the modified retrospective approach. The adoption of the guidance had no material impact on the measurement or recognition of revenue as approximately 89% of the Company's revenue (based on 2017 audited financial results) is outside the scope of this guidance; however, additional disclosures have been added in accordance with the ASU. See Note 1 for additional information on this new accounting standard.

Descriptions of our revenue-generating contracts with customers that are within the scope of ASU 2014 09, which are presented in our income statements as components of non-interest income are as follows:

Trust department and Investment advisory and management fees: This is a contract between the Company and its customers for fiduciary and/or investment administration services on trust and brokerage accounts. Trust services and brokerage fee income is determined as a percentage of assets under management and is recognized over the period the underlying trust account is serviced. Such contracts are generally cancellable at any time, with the customer subject to a pro-rated fee in the month of termination.

Deposit service fees: The deposit contract obligates the Company to serve as a custodian of the customer's deposited funds and is generally terminable at will by either party. The contract permits the customer to access the funds on deposit and request additional services related to the deposit account. Deposit account related fees, including analysis charges, overdraft/nonsufficient fund charges, service charges, debit card usage fees, overdraft fees and wire transfer fees are within the scope of the guidance; however, revenue recognition practices did not change under the guidance, as deposit agreements are considered day-to-day contracts. Income for deposit accounts is recognized over the statement cycle period (typically on a monthly basis) or at the time the service is provided, if additional services are requested.

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Correspondent banking fees: A contract between the Company and its correspondent banks for corresponding banking services. This line of business provides a strong source of noninterest bearing and interest bearing deposits, fee income, high-quality loan participations and bank stock loans. Correspondent banking fee income is tied to transaction activity and revenue is recognized monthly as earned for services provided.

NOTE 10 –MERGERS AND ACQUISITIONS

BATES COMPANIES

On March 20, 2018 the Company announced the signing of definitive agreements to acquire the Bates Companies, headquartered in Rockford, Illinois. The acquisition and subsequent merger of the Bates Companies into RB&T will enhance the wealth management services of RB&T by adding approximately $700.0 million of assets under management.

In the acquisition, the Company will acquire 100% of the Bates Companies' outstanding common stock for an aggregate consideration of $3.0 million cash and up to $3.0 million of the Company's common stock. In a private placement exempt from registration with the SEC, the Company expects to issue upon closing of the transaction approximately 21,528 common shares or $1.0 million of Company stock. Assuming all future performance based contingent consideration is realized total stock consideration can reach $3.0 million, which would result in the Company expecting to issue approximately 64,583 common shares based on closing stock price at the date of announcement.

This transaction is subject to regulatory approval and certain closing conditions. The transaction is expected to close early in fourth quarter of 2018.

SPRINGFIELD BANCSHARES, INC.

On July 1, 2018, the Company completed its previously announced merger with Springfield Bancshares, the holding company of SFC Bank, headquartered in Springfield, Missouri. SFC Bank is a Missouri-chartered bank that operates one location in the Springfield, Missouri market. As a result of the transaction, SFC Bank became the Company’s fifth independent charter.

Stockholders of Springfield Bancshares received 0.3060 shares of the Company’s common stock and $1.50 in cash in exchange for each common share of Springfield Bancshares held. On June 29, 2018, the last trading date before the closing, the Company’s common stock closed at $47.45, resulting in stock consideration valued at $79.2 million and total consideration paid by the Company of $87.4 million. To help fund the cash portion of the purchase price, on June 29, 2018, the Company borrowed $4.1 million on its existing $10.0 million revolving line of credit. The Company also borrowed $4.9 million on this same revolving line of credit to fund the repayment of certain debt assumed in the merger, shortly after closing. This note is included within other borrowings on the June 30, 2018 Consolidated Balance Sheet. The remaining cash consideration paid to the shareholders of Springfield Bancshares came from operating cash.

As of the merger date, SFC Bank had assets with a historical book value of $573 million, loans with a book value of $487 million, and deposits with a book value of $439 million. The Company is in the process of determining the fair value of the individual assets and liabilities purchased/assumed, including goodwill and core deposit intangible.

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Item 2

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

INTRODUCTION

This section reviews the financial condition and results of operations of the Company and its subsidiaries as of and for the three months ending June 30, 2018. Some tables may include additional periods to comply with disclosure requirements or to illustrate trends. When reading this discussion, also refer to the Consolidated Financial Statements and related notes in this report. The page locations and specific sections and notes that are referred to are presented in the table of contents.

Additionally, a comprehensive list of the acronyms and abbreviations used throughout this discussion is included in Note 1 to the Consolidated Financial Statements.

GENERAL

QCR Holdings, Inc. is a financial holding company and the parent company of QCBT, CRBT, CSB, RB&T and SFC Bank.

QCBT, CRBT and CSB are Iowa-chartered commercial banks, RB&T is an Illinois-chartered commercial bank and SFC Bank is a Missouri-chartered commercial bank. All are members of the Federal Reserve system with depository accounts insured to the maximum amount permitted by law by the FDIC.

· QCBT commenced operations in 1994 and provides full-service commercial and consumer banking, and trust and asset management services to the Quad City area and adjacent communities through its five offices that are located in Bettendorf and Davenport, Iowa and Moline, Illinois. QCBT also provides leasing services through its wholly-owned subsidiary, m2, located in Brookfield, Wisconsin. In addition, QCBT owns 100% of Quad City Investment Advisors, LLC, which is an investment management and advisory company.
· CRBT commenced operations in 2001 and provides full-service commercial and consumer banking, and trust and asset management services to Cedar Rapids, Iowa and adjacent communities through its five offices located in Cedar Rapids and Marion, Iowa. Cedar Falls and Waterloo, Iowa and adjacent communities are served through three additional CRBT offices (two in Waterloo and one in Cedar Falls).
· CSB was acquired by QCR in 2016, as further described in Note 2 to the Consolidated Financial Statements included in the Annual Report on Form 10 K for the year ended December 31, 2017. CSB provides full-service commercial and consumer banking to the Des Moines, Iowa area and adjacent communities through its 10 offices, including its main office located on North Ankeny Boulevard in Ankeny, Iowa.
· RB&T commenced operations in January 2005 and provides full-service commercial and consumer banking, and trust and asset management services to Rockford, Illinois and adjacent communities through its main office located on Guilford Road at Alpine Road in Rockford and its branch facility in downtown Rockford.
· The financial results of SFC Bank are not included in this report because the Company's acquisition of SFC Bank through merger of Springfield Bancshares, previously the holding company of SFC Bank, into the Company occurred on July 1, 2018.

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EXECUTIVE OVERVIEW

The Company reported net income of $10.4 million and diluted EPS of $0.73 for the quarter ended June 30, 2018. By comparison, for the quarter ended March 31, 2018, the Company reported net income of $10.6 million and diluted EPS of $0.74. For the quarter ended June 30, 2017, the Company reported net income of $8.8 million and diluted EPS of $0.65. For the six months ended June 30, 2018, the Company reported net income of $21.0 million, and diluted EPS of $1.48. By comparison, for the six months ended June 30, 2017, the Company reported net income of $18.0 million, and diluted EPS of $1.33.

The second quarter of 2018 was highlighted by several significant items:

· Net income of $10.4 million, or $0.73 per diluted share;
· Core net income (non-GAAP) of $10.9 million, or $0.77 per diluted share;
· Annualized loan and lease growth of 7.8% for the quarter ended and 10.1% year-to-date; and
· Annualized noninterest income growth of 17.4%.

Following is a table that represents various net income measurements for the Company.

	For the three months ended			For the six months ended	
	June 30, 2018	December 31, 2017	June 30, 2017	June 30, 2018	June 30, 2017
Net income	$ 10,445,385	$ 9,901,590	$ 8,766,017	$ 20,995,346	$ 17,950,982
Diluted earnings per common share	$ 0.73	$ 0.70	$ 0.65	$ 1.48	$ 1.33
Weighted average common and common equivalent shares outstanding	14,232,423	14,193,191	13,516,592	14,219,003	13,502,505

The increase in weighted average common shares outstanding from June 30, 2017 to June 30, 2018 was primarily due to the common stock issued to Guaranty as consideration for the acquisition of Guaranty Bank.

Following is a table that represents the major income and expense categories for the Company.

	For the three months ended			For the six months ended	
	June 30, 2018	March 31, 2018	June 30, 2017	June 30, 2018	June 30, 2017
Net interest income	$ 32,084,496	$ 32,402,918	$ 28,046,697	$ 64,487,414	$ 55,715,580
Provision expense	2,300,735	2,539,839	2,022,993	4,840,574	4,128,102
Noninterest income	8,912,266	8,541,449	6,782,518	17,453,715	14,066,272
Noninterest expense	26,369,823	25,863,497	21,404,629	52,233,320	42,677,746

Federal and state income tax expense	1,880,819	1,991,070	2,635,576	3,871,889	5,025,022
Net income	$ 10,445,385	$ 10,549,961	$ 8,766,017	$ 20,995,346	$ 17,950,982

Following are some noteworthy changes in the Company's financial results:

· Net interest income in the second quarter of 2018 was down 1% compared to the first quarter of 2018. Net interest income increased 14% compared to the second quarter of 2017 and 16% when comparing the first six months of 2018 to the same period in the prior year. This increase was primarily due to strong loan and lease growth and the acquisition of Guaranty Bank.

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- Provision expense in the second quarter of 2018 decreased 9% compared to the first quarter of 2018 and increased 14% from the same period of 2017. Provision expense increased 17% in the first six months of 2018 from the same period of 2017 and was attributable to both strong loan growth and accounting for acquired loans. As acquired loans renew, the discount associated with those loans is eliminated and the Company must establish an allowance.
- Noninterest income in the second quarter of 2018 increased 4% compared to the first quarter of 2018, primarily due to higher swap fee income. Noninterest income in the second quarter of 2018 increased 31% from the second quarter of 2017 and 24% when comparing the first six months of 2018 to the same period in the prior year. This increase was primarily attributable to higher swap fee income, as well as solid growth in wealth management fee income and the acquisition of Guaranty Bank.
- Noninterest expense increased 2% from the first quarter of 2018. Noninterest expense increased 23% from the second quarter of 2017 and 22% when comparing the first six months of 2018 to the same period in the prior year which was primarily due to the acquisition of Guaranty Bank.
- Federal and state income tax expense in the second quarter of 2018 decreased 6% compared to the first quarter of 2018. Federal and state income tax expense in the second quarter of 2018 decreased 29% compared to the second quarter of 2017 and decreased 23% when comparing the first six months of 2018 to the same period in the prior year primarily due to a lower federal tax rate. See the "Income Taxes" section of this Report for additional details.

LONG-TERM FINANCIAL GOALS

As previously stated, the Company has established certain financial goals by which it manages its business and measures its performance. The goals are periodically updated to reflect changes in business developments. While the Company is determined to work prudently to achieve these goals, there is no assurance that they will be met. Moreover, the Company's ability to achieve these goals will be affected by the factors discussed under "Forward Looking Statements" as well as the factors detailed in the "Risk Factors" section included under Item 1A. of Part I of the Company's Annual Report on Form 10 K for the year ended December 31, 2017. The Company's long-term financial goals are as follows:

- Improve balance sheet efficiency by maintaining a gross loans and leases to total assets ratio in the range of 73 – 78%;
- Improve profitability (measured by NIM and ROAA);
- Improve asset quality by reducing NPAs to total assets to below 0.75% and maintain charge-offs as a percentage of average loans/leases of under 0.25% annually;
- Maintain reliance on wholesale funding at less than 15% of total assets;
- Grow noninterest bearing deposits to more than 30% of total assets;
- Continue to focus on generating gains on sales of government guaranteed portions of loans and swap fee income to more than $4 million annually; and
- Grow wealth management segment net income by 10% annually.

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The following table shows the evaluation of the Company's long-term financial goals.

			For the Quarter Ending		
Goal	Key Metric	Target**	June 30, 2018	March 31, 2018	June 30, 2017
Balance sheet efficiency	Gross loans and leases to total assets	73% - 78%	76 %	76 %	74 %
	NIM TEY (non-GAAP)*	> 3.65%	3.52 %	3.64 %	3.81 %
Profitability	ROAA	> 1.10%	1.03 %	1.06 %	1.04 %
	Core ROAA (non-GAAP)*	> 1.10%	1.08 %	1.06 %	1.04 %
Asset quality	NPAs to total assets	< 0.75%	0.65 %	0.77 %	0.75 %
	Net charge-offs to average loans and leases***	< 0.25% annually	0.11 %	0.05 %	0.13 %
Reliance on wholesale funding	Wholesale funding to total assets****	< 15%	13 %	14 %	10 %
Funding mix	Noninterest bearing deposits as a percentage of total assets	> 30%	18 %	19 %	22 %
Consistent, high quality noninterest income revenue streams	Gains on sales of government guaranteed portions of loans and swap fee income***	> $4 million annually	$ 5.9 million	$ 5.3 million	$ 3.0 million
	Grow wealth management segment net income***	> 10% annually	54 %	37 %	22 %

* See "GAAP to Non-GAAP" reconciliations section.

** Targets will be re-evaluated and adjusted as appropriate.

*** Ratios and amounts provided for these measurements represent year-to-date actual amounts for the respective period, that are then annualized for comparison.

**** Wholesale funding to total assets is calculated by dividing total borrowings and brokered deposits by total assets.

STRATEGIC DEVELOPMENTS

The Company took the following actions during the second quarter of 2018 to support its corporate strategy and the long-term financial goals shown above.

- The Company grew loans and leases in the second quarter of 2018 by 7.8% on an annualized basis. Strong loan and lease growth for the remainder of the year will help keep the Company's loan and leases to asset ratio within the targeted range of 73 78%.

- The Company has participated, and intends to continue to participate, in a prudent manner as an acquirer in the consolidation taking place in our markets to continue to grow EPS, further boost ROAA and improve the Company's efficiency ratio. The Company announced in March 2018 the signing of definitive agreements to acquire and merge the Bates Companies into RB&T. The Company announced in July 2018 the completion of the merger of Springfield Bancshares. See Note 10 to the Consolidated Financial Statements for additional details about these strategic transactions.
- The Company has continued to focus on lowering the NPAs to total assets ratio. This ratio decreased by 12 basis points to 0.65%, compared to the first quarter 2018. This decrease was primarily due to the upgrade of one large credit that was taken out of TDR status. The Company remains committed to improving asset quality ratios in 2018 and beyond.
- Management has continued to focus on reducing the Company's reliance on wholesale funding. Core deposit growth in the second quarter of 2018 allowed wholesale funding to decrease 1%. Management continues to prioritize core deposit growth through a variety of strategies including growth in correspondent banking.

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- Correspondent banking has continued to be a core line of business for the Company. The Company is competitively positioned with experienced staff, software systems and processes to continue growing in the three states currently served – Iowa, Illinois and Wisconsin - and to expand into the Missouri market. The Company acts as the correspondent bank for 192 downstream banks with average total noninterest bearing deposits of $215.3 million that hadaverage total interest bearing deposits of $208.3 million during the first six months of 2018. This line of business provides a strong source of noninterest bearing and interest bearing deposits, fee income, high-quality loan participations and bank stock loans.
- SBA and USDA lending is a specialty lending area on which the Company has focused. Once these loans are originated, the government-guaranteed portion of the loan can be sold to the secondary market for premiums.
- As a result of the relatively low interest rate environment including a flat yield curve, the Company has focused on executing interest rate swaps on select commercial loans. The interest rate swaps allow the commercial borrowers to pay a fixed interest rate while the Company receives a variable interest rate as well as an upfront fee dependent on the pricing. Management believes that these swaps help position the Company more favorably for rising rate environments. The Company will continue to review opportunities to execute these swaps at all of its subsidiary banks, as the circumstances are appropriate for the borrower and the Company.
- Wealth management is another core line of business for the Company and includes a full range of products, including trust services, brokerage and investment advisory services, asset management, estate planning and financial planning. As of June 30, 2018, the Company had $2.72 billion of total financial assets in trust (and related) accounts and $1.05 billion of total financial assets in brokerage (and related) accounts. Continued growth in assets under management will help drive trust and investment advisory fees. The Company offers trust and investment advisory services to the correspondent banks that it serves. As management continues to focus on growing wealth management fee income, expanding market share will continue to be a primary strategy, both through organic growth as well as the acquisition of managed assets. The Company announced in March 2018 the signing of definitive agreements to acquire and merge the Bates Companies into RB&T. The acquisition and subsequent merger of the Bates Companies into RB&T will add approximately $700 million of assets under management.

GAAP TO NON-GAAP RECONCILIATIONS

The following table presents certain non-GAAP financial measures related to the "TCE/TA ratio", "core net income", "core net income attributable to QCR Holdings, Inc. common stockholders", "core EPS", "core ROAA", "NIM (TEY)", and "efficiency ratio". In compliance with applicable rules of the SEC, all non-GAAP measures are reconciled to the most directly comparable GAAP measure, as follows:

- TCE/TA ratio (non-GAAP) is reconciled to stockholders' equity and total assets;
- Core net income, core net income attributable to QCR Holdings, Inc. common stockholders, core EPS and core ROAA (all non-GAAP measures) are reconciled to net income;
- NIM (TEY) (non-GAAP) is reconciled to NIM; and
- Efficiency ratio (non-GAAP) is reconciled to noninterest expense, net interest income and noninterest income.

The TCE/TA non-GAAP ratio has been a focus for investors and management believes that this ratio may assist investors in analyzing the Company's capital position without regard to the effects of intangible assets.

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The table following also includes several "core" non-GAAP measurements of financial performance. The Company's management believes that these measures are important to investors as they exclude non-recurring income and expense items; therefore, they provide a better comparison for analysis and may provide a better indicator of future run-rates.

NIM (TEY) is a financial measure that the Company's management utilizes to take into account the tax benefit associated with certain tax-exempt loans and securities. It is standard industry practice to measure net interest margin using tax-equivalent measures.

The efficiency ratio is a ratio that management utilizes to compare the Company to peers. It is a standard ratio in the banking industry and widely utilized by investors.

Non-GAAP financial measures have inherent limitations, are not required to be uniformly applied, and are not audited. Although these non-GAAP financial measures are frequently used by investors to evaluate a company, they have limitations as analytical tools and should not be considered in isolation, or as a substitute for analyses of results as reported under GAAP.

GAAP TO NON-GAAP RECONCILIATIONS	As of June 30, 2018	March 31, 2018	December 31, 2017	September 30, 2017	June 30, 2017
	(dollars in thousands, except per share data)				
TCE/TA RATIO					
Stockholders' equity (GAAP)	$ 369,588	$ 360,428	$ 353,287	$ 313,039	$ 305,083
Less: Intangible assets	36,561	37,108	37,413	19,800	20,030
TCE (non-GAAP)	$ 333,027	$ 323,320	$ 315,874	$ 293,239	$ 285,053
Total assets (GAAP)	$ 4,106,883	$ 4,026,314	$ 3,982,665	$ 3,550,463	$ 3,457,187
Less: Intangible assets	36,561	37,108	37,413	19,800	20,030
TA (non-GAAP)	$ 4,070,322	$ 3,989,206	$ 3,945,252	$ 3,530,663	$ 3,437,157
TCE/TA ratio (non-GAAP)	8.18 %	8.10 %	8.01 %	8.31 %	8.29 %

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	For the Quarter Ended			For the Six Months Ended	
	June 30, 2018	March 31, 2018	December 31, 2017	June 30, 2018	June 30, 2017
	(dollars in thousands,except per share data)				
CORE NET INCOME					
Net income (GAAP)	$ 10,445	$ 10,550	$ 9,902	$ 20,995	$ 17,951
Less nonrecurring items (post-tax) (*):					
Income:					
Securities gains, net	$ —	$ —	$ (41)	$ —	$ 25
Total nonrecurring income (non-GAAP)	$ —	$ —	$ (41)	$ —	$ 25
Expense:					
Acquisition costs	$ 327	$ 73	$ 430	$ 400	$ —
Post-acquisition compensation, transition and integration costs	130	—	2,462	130	—
Total nonrecurring expense (non-GAAP)	$ 457	$ 73	$ 2,892	$ 530	$ —
Adjustment of tax expense related to the Tax Act	$ —	$ —	$ 2,919	$ —	$ —
Core net income (non-GAAP)	$ 10,902	$ 10,623	$ 9,916	$ 21,525	$ 17,926

CORE EPS

Core net income (non-GAAP) (from above)	$ 10,902	$ 10,623	$ 9,916	$ 21,525	$ 17,926
Weighted average common shares outstanding	13,919,565	13,888,661	13,845,497	13,904,113	13,151,833
Weighted average common and common equivalent shares outstanding	14,232,423	14,205,584	14,193,191	14,219,003	13,502,505
Core EPS (non-GAAP):					
Basic	$ 0.78	$ 0.76	$ 0.72	$ 1.55	$ 1.36
Diluted	$ 0.77	$ 0.75	$ 0.70	$ 1.51	$ 1.33
CORE ROAA					
Core net income (non-GAAP) (from above)	$ 10,902	$ 10,623	$ 9,916	$ 21,525	$ 17,926
Average Assets	$ 4,053,684	$ 3,994,691	$ 3,923,337	$ 4,024,188	$ 3,326,454
Core ROAA (annualized) (non-GAAP)	1.08 %	1.06 %	1.01 %	1.07 %	1.08 %
NIM (TEY)*					
Net interest income (GAAP)	$ 32,085	$ 32,403	$ 31,793	$ 64,488	$ 55,716
Plus: Taxequivalent adjustment	1,462	1,353	2,585	2,815	4,218
Net interest income - taxequivalent (non-GAAP)	$ 33,547	$ 33,756	$ 34,378	$ 67,303	$ 59,934
Average earning assets	$ 3,820,333	$ 3,759,475	$ 3,699,193	$ 3,789,905	$ 3,128,569
NIM (GAAP)	3.37 %	3.50 %	3.41 %	3.43 %	3.59 %
NIM (TEY) (non-GAAP)	3.52 %	3.64 %	3.69 %	3.58 %	3.86 %
EFFICIENCY RATIO					
	$ 26,370	$ 25,863	$ 31,351	$ 52,234	$ 42,678

Noninterest expense (GAAP)										
Net interest income (GAAP)	$ 32,085		$ 32,403		$ 31,793		$ 64,488		$ 55,716	
Noninterest income (GAAP)	8,912		8,541		9,714		17,454		14,066	
Total income	$ 40,997		$ 40,944		$ 41,507		$ 81,942		$ 69,782	
Efficiency ratio (noninterest expense/total income) (non-GAAP)	64.32	%	63.17	%	75.53	%	63.75	%	61.16	%

* Nonrecurring items (after-tax) are calculated using an estimated effective tax rate of 35% for periods prior to March 31, 2018 and 21% for periods including and after March 31, 2018.

NET INTEREST INCOME - (TAX EQUIVALENT BASIS)

As part of the Tax Act, the Company's federal income tax rate was reduced from 35% down to 21% effective January 1, 2018. In order to compare periods before and after the effective date of the Tax Act, it's important to note the difference in the federal income tax rate and the impact on the Company's tax exempt earning assets (loans and securities) and the related tax equivalent yield reporting.

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Net interest income, on a tax equivalent basis, increased 11% to $33.5 million for the quarter ended June 30, 2018, compared to the same quarter of the prior year, and increased 12% to $67.3 million for the six months ended June 30, 2018 compared to the same period of the prior year. Excluding the tax equivalent adjustments, net interest income increased 14% for the quarter ended June 30, 2018 compared to the same quarter of the prior year, and increased 16% for the six months ended June 30, 2018 compared to the same period of the prior year. Net interest income improved due to several factors:

- Organic loan and lease growth has been strong over the past 12 months pushing loans/leases up to 76% of total assets;
- The acquisition of Guaranty Bank in the fourth quarter of 2017, whose strong NIM has contributed to the Company's results; and
- The Company's continued strategy to redeploy funds from the lower yielding taxable securities portfolio into higher yielding loans and municipal bonds, especially with the Company's most recent acquisitions of CSB and Guaranty Bank.

A comparison of yields, spread and margin on a tax equivalent and GAAP basis is as follows:

	Tax Equivalent Basis For the Quarter Ended						GAAP For the Quarter Ended					
	June 30, 2018		March 31, 2018		June 30, 2017		June 30, 2018		March 31, 2018		June 30, 2017	
Average Yield on Interest-Earning Assets	4.44	%	4.41	%	4.37	%	4.28	%	4.27	%	4.09	%
Average Cost of Interest-Bearing Liabilities	1.21	%	1.03	%	0.77	%	1.21	%	1.03	%	0.77	%
Net Interest Spread	3.23	%	3.38	%	3.60	%	3.07	%	3.24	%	3.32	%
NIM	3.52	%	3.64	%	3.81	%	3.37	%	3.50	%	3.54	%
NIM Excluding Acquisition Accounting Net Accretion	3.46	%	3.56	%	3.61	%	3.31	%	3.42	%	3.34	%

	Tax Equivalent Basis For the Six Months Ended				GAAP For the Six Months Ended			
	June 30, 2018		June 30, 2017		June 30, 2018		June 30, 2017	
Average Yield on Interest-Earning Assets	4.42	%	4.38	%	4.28	%	4.11	%
Average Cost of Interest-Bearing Liabilities	1.13	%	0.73	%	1.13	%	0.73	%
Net Interest Spread	3.29	%	3.65	%	3.15	%	3.38	%
NIM	3.58	%	3.86	%	3.43	%	3.59	%

NIM Excluding Acquisition Accounting Net Accretion	3.51 %	3.63 %	3.37 %	3.36 %

Acquisition accounting net accretion can fluctuate depending on the payoff activity of the acquired loans. In evaluating net interest income and NIM, it's important to understand the impact of acquisition accounting net accretion when comparing periods. The above table reports NIM with and without the acquisition accounting net accretion to allow for more appropriate comparisons. A comparison of acquisition accounting net accretion included in NIM is as follows:

	For the Quarter Ended			For the Six Months Ended	
	June 30, 2018	March 31, 2018	June 30, 2017	June 30, 2018	June 30, 2017
	dollars in thousands				
Acquisition Accounting Net Accretion in NIM	$ 545	$ 699	$ 1,553	$ 1,244	$ 3,584

NIM on a tax equivalent basis was down 12 basis points on a linked quarter basis. . Excluding acquisition accounting net accretion, NIM was down 10 basis points on a linked quarter basis. This margin compression was primarily due to the following:

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- Increases in the cost of funds due to both mix and rate as the Company continues to grow larger commercial and public deposits which tend to have higher interest rate sensitivity;
- In the first quarter of 2018, the Company recognized elevated loan origination fee income through NIM for select commercial loans which contributed to approximately five basis points of the core NIM decline;
- With the flat yield curve and continued competition in our markets, loan pricing continues to be pressured. The Company had success in widening spreads as core loan yields increased 13 basis points on linked quarter basis; however, the pace and magnitude of the widening has been offset by the increasing cost of funds;
- The majority of the Company's earning asset growth in the second quarter of 2018 occurred at the end of the quarter.

The Company's management closely monitors and manages NIM. From a profitability standpoint, an important challenge for the Company's subsidiary banks and leasing company is focusing on quality growth in conjunction with the improvement of their NIMs. Management continually addresses this issue with pricing and other balance sheet management strategies which included better loan pricing, reducing reliance on very rate-sensitive funding, closely managing deposit rate increases and finding additional ways to manage cost of funds through derivatives.

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The Company's average balances, interest income/expense, and rates earned/paid on major balance sheet categories, as well as the components of change in net interest income, are presented in the following tables:

	For the three months ended June 30, 2018			2017		
	Average Balance	Interest Earned or Paid	Average Yield or Cost	Average Balance	Interest Earned or Paid	Average Yield or Cost
	(dollars in thousands)					
ASSETS						
Interest earning assets:						
Federal funds sold	$ 18,561	$ 61	1.32 %	$ 18,742	$ 38	0.81 %
Interest-bearing deposits at financial institutions	54,879	228	1.67 %	86,236	220	1.02 %
Investment securities (1)	648,276	5,752	3.56 %	573,747	5,384	3.76 %
Restricted investment securities	21,100	212	4.03 %	13,226	132	4.00 %
Gross loans/leases receivable (1) (2) (3)	3,077,517	36,008	4.69 %	2,488,828	28,881	4.65 %
Total interest earning assets	$ 3,820,333	$ 42,261	4.44 %	$ 3,180,779	$ 34,655	4.37 %
Noninterest-earning assets:						
Cash and due from banks	$ 68,266			$ 63,526		
Premises and equipment	63,665			61,327		
Less allowance	(36,960)			(32,361)		
Other	138,380			104,924		
Total assets	$ 4,053,684			$ 3,378,195		
LIABILITIES AND STOCKHOLDERS' EQUITY						
Interest-bearing liabilities:						
Interest-bearing deposits	$ 1,919,406	4,089	0.85 %	$ 1,566,106	1,835	0.47 %
Time deposits	665,643	2,439	1.47 %	527,719	1,156	0.88 %
Short-term borrowings	19,024	63	1.33 %	17,936	19	0.42 %
FHLB advances	174,826	882	2.02 %	76,739	354	1.85 %
Other borrowings	67,044	733	4.39 %	72,000	696	3.88 %
	37,558	508	5.43 %	33,530	347	4.15 %

Junior subordinated debentures						
Total interest-bearing liabilities	$ 2,883,501	$ 8,714	1.21 %	$ 2,294,030	$ 4,407	0.77 %
Noninterest-bearing demand deposits	$ 757,954			$ 741,886		
Other noninterest-bearing liabilities	47,198			41,411		
Total liabilities	$ 3,688,653			$ 3,077,327		
Stockholders' equity	365,031			300,868		
Total liabilities and stockholders' equity	$ 4,053,684			$ 3,378,195		
Net interest income		$ 33,547			$ 30,248	
Net interest spread			3.23 %			3.60 %
Net interest margin			3.52 %			3.81 %
Ratio of average interest-earning assets to average interest-bearing liabilities	132.49 %			138.65 %		

(1) Interest earned and yields on nontaxable investment securities and nontaxable loans are determined on a tax equivalent basis using a 35% tax rate for periods prior to March 31, 2018 and 21% for periods including and after March 31, 2018.
(2) Loan/lease fees are not material and are included in interest income from loans/leases receivable in accordance with accounting and regulatory guidance.
(3) Non-accrual loans/leases are included in the average balance for gross loans/leases receivable in accordance with accounting and regulatory guidance.

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MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS - continued

Analysis of Changes of Interest Income/Interest Expense

For the three months ended June 30, 2018

	Inc./(Dec.) from Prior Period	Components of Change (1)	
		Rate	Volume
	2018 vs. 2017		
	(dollars in thousands)		
INTEREST INCOME			
Federal funds sold	$ 23	$ 25	$ (2)
Interest-bearing deposits at financial institutions	8	412	(404)
Investment securities (2)	368	(1,549)	1,917
Restricted investment securities	80	1	79
Gross loans/leases receivable (2) (3) (4)	7,127	241	6,886
Total change in interest income	$ 7,606	$ (870)	$ 8,476
INTEREST EXPENSE			
Interest-bearing deposits	$ 2,254	$ 1,767	$ 487
Time deposits	1,283	924	359
Short-term borrowings	44	43	1
Federal Home Loan Bank advances	528	36	492
Other borrowings	37	276	(239)
Junior subordinated debentures	161	116	45
Total change in interest expense	$ 4,307	$ 3,162	$ 1,145
Total change in net interest income	$ 3,299	$ (4,032)	$ 7,331

(1) The column "Inc./(Dec.) from Prior Period" is segmented into the changes attributable to variations in volume and the changes attributable to changes in interest rates. The variations attributable to simultaneous volume and rate changes have been proportionately allocated to rate and volume.
(2) Interest earned and yields on nontaxable investment securities and nontaxable loans are determined on a tax equivalent basis using a 35% tax rate for periods prior to March 31, 2018 and 21% for periods including and after March 31, 2018.
(3) Loan/lease fees are not material and are included in interest income from loans/leases receivable in accordance with accounting and regulatory guidance.
(4) Non-accrual loans/leases are included in the average balance for gross loans/leases receivable in accordance with accounting and regulatory guidance.

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MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS - continued

	For the six months ended June 30, 2018			2017		
	Average Balance	Interest Earned or Paid	Average Yield or Cost	Average Balance	Interest Earned or Paid	Average Yield or Cost
ASSETS						
Interest earning assets:						
Federal funds sold	$ 19,132	$ 118	1.24 %	$ 14,917	$ 53	0.72 %
Interest-bearing deposits at financial institutions	52,205	425	1.64	89,394	418	0.94 %
Investment securities (1)	648,656	11,418	3.55	567,101	10,543	3.75 %
Restricted investment securities	21,465	446	4.19	13,549	262	3.90 %
Gross loans/leases receivable (1) (2) (3)	3,048,447	70,753	4.68	2,443,608	56,741	4.68 %
Total interest earning assets	$ 3,789,905	83,160	4.42	$ 3,128,569	68,017	4.38 %
Noninterest-earning assets:						
Cash and due from banks	$ 67,745			$ 64,409		
Premises and equipment, net	63,530			61,152		
Less allowance for estimated losses on loans/leases	(36,048)			(31,930)		
Other	139,057			104,256		
Total assets	$ 4,024,189			$ 3,326,456		
LIABILITIES AND STOCKHOLDERS' EQUITY						
Interest-bearing liabilities:						
Interest-bearing demand deposits	$ 1,873,817	7,109	0.77 %	$ 1,486,876	2,974	0.40 %
Time deposits	641,152	4,301	1.35	519,419	2,249	0.87 %
Short-term borrowings	18,148	95	1.06	21,562	43	0.40 %

Federal Home Loan Bank advances	205,758	1,946	1.91	95,548	758	1.60 %
Other borrowings	65,862	1,451	4.44	73,381	1,379	3.79 %
Junior subordinated debentures	37,534	955	5.13	33,514	680	4.09 %
Total interest-bearing liabilities	$ 2,842,271	15,857	1.13	$ 2,230,300	8,083	0.73 %
Noninterest-bearing demand deposits	$ 776,314			$ 757,566		
Other noninterest-bearing liabilities	44,826			42,704		
Total liabilities	$ 3,663,411			$ 3,030,569		
Stockholders' equity	360,778			295,887		
Total liabilities and stockholders' equity	$ 4,024,189			$ 3,326,456		
Net interest income		$ 67,303			$ 59,934	
Net interest spread			3.29 %			3.65 %
Net interest margin			3.58 %			3.86 %
Ratio of average interest earning assets to average interest-bearing liabilities	133.34 %			140.28 %		

(1) Interest earned and yields on nontaxable investment securities and nontaxable loans are determined on a tax equivalent basis using a 35% tax rate for periods prior to March 31, 2018 and 21% for periods including and after March 31, 2018.
(2) Loan/lease fees are not material and are included in interest income from loans/leases receivable in accordance with accounting and regulatory guidance.
(3) Non-accrual loans/leases are included in the average balance for gross loans/leases receivable in accordance with accounting and regulatory guidance.

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Analysis of Changes of Interest Income/Interest Expense
For the six months ended June 30, 2018

	Inc./(Dec.) from Prior Period	Components of Change (1)	
		Rate	Volume
	2018 vs. 2017		
	(dollars in thousands)		
INTEREST INCOME			
Federal funds sold	$ 65	$ 47	$ 18
Interest-bearing deposits at other financial institutions	7	454	(447)
Investment securities (2)	875	(1,414)	2,289
Restricted investment securities	184	21	163
Gross loans/leases receivable (2) (3) (4)	14,012	(80)	14,092
Total change in interest income	$ 15,143	$ (972)	$ 16,115
INTEREST EXPENSE			
Interest-bearing demand deposits	$ 4,135	$ 3,205	$ 930
Time deposits	2,052	1,438	614
Short-term borrowings	52	73	(21)
Federal Home Loan Bank advances	1,188	170	1,018
Other borrowings	72	403	(331)
Junior subordinated debentures	275	(40)	315
Total change in interest expense	$ 7,774	$ 5,249	$ 2,525
Total change in net interest income	$ 7,369	$ (6,221)	$ 13,590

(1) The column "Inc./(Dec.) from Prior Period" is segmented into the changes attributable to variations in volume and the changes attributable to changes in interest rates. The variations attributable to simultaneous volume and rate changes have been proportionately allocated to rate and volume.
(2) Interest earned and yields on nontaxable investment securities and nontaxable loans are determined on a tax equivalent basis using a 35% tax rate for periods prior to March 31, 2018 and 21% for periods including and after March 31, 2018.
(3) Loan/lease fees are not material and are included in interest income from loans/leases receivable in accordance with accounting and regulatory guidance.
(4) Non-accrual loans/leases are included in the average balance for gross loans/leases receivable in accordance with accounting and regulatory guidance.

CRITICAL ACCOUNTING POLICIES

The Company's financial statements are prepared in accordance with GAAP. The financial information contained within these statements is, to a significant extent, financial information that is based on approximate measures of the financial effects of transactions and events that have already occurred. Certain critical accounting policies are described below.

ALLOWANCE FOR LOAN AND LEASE LOSSES

Based on its consideration of accounting policies that involve the most complex and subjective decisions and assessments, management has identified its most critical accounting policy to be that related to the allowance for loan and lease losses.

The Company's allowance methodology incorporates a variety of risk considerations, both quantitative and qualitative, in establishing an allowance that management believes is appropriate at each reporting date. Quantitative factors include the Company's historical loss experience, delinquency and charge-off trends, collateral values, changes in NPLs, and other factors. Quantitative factors also incorporate known information about individual loans/leases, including borrowers' sensitivity to interest rate movements.

Qualitative factors include management's view regarding the general economic environment in the Company's markets, including economic conditions throughout the Midwest and, in particular, the state of certain industries. Size and

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complexity of individual credits in relation to loan/lease structures, existing loan/lease policies and pace of portfolio growth are other qualitative factors that are considered in the methodology.

Management may report a materially different amount for the provision in the statement of income to change the allowance if its assessment of the above factors were different. This discussion and analysis should be read in conjunction with the Company's financial statements and the accompanying notes presented elsewhere herein, as well as the section entitled “Financial Condition” of this Management's Discussion and Analysis that discusses the allowance.

Although management believes the level of the allowance as of June 30, 2018 was adequate to absorb losses in the loan/lease portfolio, a decline in local economic conditions, or other factors, could result in increasing losses that cannot be reasonably predicted at this time.

RESULTS OF OPERATIONS

INTEREST INCOME

Interest income increased 26%, comparing the second quarter of 2018 to the same period of 2017 and comparing the first half of 2018 to the same period of 2017. This increase was primarily the result of strong organic loan growth, the acquisition of Guaranty Bank, and improved pricing with the rising rate environment. Although the latter has been less than the Company would like due to competitive pressures and the flat yield cureve, the Company is focused on growing loans at higher rates with widening spreads to more than effect the rising cost of funds

Overall, the Company's average earning assets increased 20%, comparing the second quarter of 2018 to the second quarter of 2017. During the same time period, average gross loans and leases increased 24%, while average investment securities increased 13% with a portion being private placement tax-exempt municipal securities. Average earning assets increased 21%, comparing the first half of 2018 to the same period of 2017. Average gross loans and leases increased 25% and average investment securities increased 14%, comparing the first half of 2018 to the same period to 2017. These increases were also the result of strong loan growth and the acquisition of Guaranty Bank.

The Company intends to continue to grow quality loans and leases as well as its private placement tax-exempt securities portfolio to maximize yield while minimizing credit and interest rate risk.

INTEREST EXPENSE

Interest expense for the second quarter of 2018 increased 98% from the second quarter of 2017 and increased 96%, comparing the first half of 2018 to the same period of 2017. The acquisition of Guaranty Bank contributed to this increase as we added over $200MM in deposits. Additionally, as the Company has grown organically at a significant pace over the past several years, the loan growth has been funded in larger part by bigger depositor relationships with higher rate sensitivity and many of those relationships which have pricing tied to a certain index. As a result, the cost of these funds is higher than the rest of the Company’s core deposit portfolio, and the cost rises at a higher rate (beta) as market interest rates rise which has been the case over the past several quarters. The beta on the balance of the Company’s core deposit portfolio has performed well and is much lower than the beta on these relationships with pricing tied to a certain index. Additionally, the loan growth has outpaced deposit growth, short-term borrowings have increased to fill in the funding gap and the cost of these funds has increased with the rising rate environment.

The Company's management intends to continue to shift the mix of funding from wholesale funds to well-priced core deposits, including noninterest-bearing deposits. Continuing this trend is expected to strengthen the Company's franchise value, reduce funding costs, and increase fee income opportunities through deposit service charges.

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PROVISION FOR LOAN/LEASE LOSSES

The provision is established based on a number of factors, including the Company's historical loss experience, delinquencies and charge-off trends, the local and national economy and risk associated with the loans/leases in the portfolio as described in more detail in the “Critical Accounting Policies” section.

The Company's provision totaled $2.3 million for the second quarter of 2018, which was an increase of $278 thousand or 14% from the same quarter of the prior year. Provision for the first six months of the year totaled $4.8 million, which was up $712 thousand or 17%, compared to the first six months of 2017. The increase from the second quarter of 2017 to the second quarter of 2018 was primarily attributable to loan growth and the accounting for the loans acquired through the acquisitions of CSB and Guaranty Bank. As acquired loans renew, the discount associated with those loans is eliminated and the Company must establish an allowance through provision. This provision, when coupled with net charge-offs of $1.7 million for the first six months of 2018, increased the Company's allowance to $37.5 million at June 30, 2018. As of June 30, 2018, the Company's allowance to total loans/leases was 1.21%, which was relatively flat from 1.20% at March 31, 2018 and down from 1.31% at June 30, 2017.

In accordance with GAAP for business combination accounting, acquired loans are recorded at fair value; therefore, no allowance is associated with such loans at acquisition. Management continues to evaluate the allowance needed on acquired loans factoring in the net remaining discount ($6.6 million and $6.3 million at June 30, 2018 and June 30, 2017, respectively). When factoring this remaining discount into the Company's allowance to total loans and leases calculation, the Company's allowance as a percentage of total loans and leases increases from 1.21% to 1.42% as of June 30, 2018 and increases from 1.31% to 1.55% as of June 30, 2017.

A more detailed discussion of the Company's allowance can be found in the “Financial Condition” section of this Report.

NONINTEREST INCOME

	Three Months Ended				
	June 30, 2018	June 30, 2017	$ Change	% Change	
Trust department fees	$ 2,057,987	$ 1,692,001	$ 365,986	21.6	%
Investment advisory and management fees	1,057,666	868,835	188,831	21.7	
Deposit service fees	1,610,403	1,458,359	152,044	10.4	
Gains on sales of residential real estate loans, net	101,772	112,628	(10,856)	(9.6)	
Gains on sales of government guaranteed portions of loans, net	—	87,053	(87,053)	(100.0)	
Swap fee income	1,648,885	327,577	1,321,308	403.4	
Securities gains, net	—	38,464	(38,464)	(100.0)	
Earnings on bank-owned life insurance	399,273	459,359	(60,086)	(13.1)	

Debit card fees	844,286	743,521	100,765	13.6	
Correspondent banking fees	212,530	200,057	12,473	6.2	
Other	979,464	794,664	184,800	23.3	
Total noninterest income	$ 8,912,266	$ 6,782,518	$ 2,129,748	31.4	%

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	Six Months Ended June 30, 2018	June 30, 2017	$ Change	% Change
Trust department fees	$ 4,295,068	$ 3,432,208	$ 862,860	25.1 %
Investment advisory and management fees	2,010,010	1,830,434	179,576	9.8
Deposit service fees	3,141,856	2,774,749	367,107	13.2
Gains on sales of residential real estate loans, net	202,587	208,951	(6,364)	(3.0)
Gains on sales of government guaranteed portions of loans, net	358,434	1,037,694	(679,260)	(65.5)
Swap fee income	2,607,579	441,097	2,166,482	491.2
Securities gains, net	—	38,464	(38,464)	(100.0)
Earnings on bank-owned life insurance	817,260	929,046	(111,786)	(12.0)
Debit card fees	1,610,394	1,446,322	164,072	11.3
Correspondent banking fees	477,357	445,246	32,111	7.2
Other	1,933,170	1,482,061	451,109	30.4
Total noninterest income	$ 17,453,715	$ 14,066,272	$ 3,387,443	24.1 %

In recent years, the Company has been successful in expanding its wealth management customer base. Trust department fees continue to be a significant contributor to noninterest income and, due to favorable market conditions in early 2018 coupled with strong growth in assets under management, trust department fees increased 22%, comparing the second quarter of 2018 to the same period of the prior year. Trust department fees increased 25% when comparing the first half of 2018 to the same period of the prior year. Income is generated primarily from fees charged based on assets under administration for corporate and personal trusts and for custodial services. The majority of the trust department fees are determined based on the value of the investments within the fully-managed trusts. Additionally, the Company started offering trust operations services to correspondent banks.

Investment advisory and management fees increased 22%, comparing the second quarter of 2018 to the same period of the prior year, and they increased 10% when comparing the first half of 2018 to the first half of 2017. Management has placed a stronger emphasis on growing its investment advisory and management services. Part of this initiative has been to restructure the Company's Wealth Management Division to allow for more efficient delivery of products and services through selective additions of talent as well as the leverage of and collaboration among existing resources (including the aforementioned trust department). Similar to trust department fees, these fees are largely determined based on the value of the investments managed. The Company announced in March 2018 the signing of definitive agreements to acquire and merge the Bates Companies into RB&T. The acquisition and subsequent merger of the Bates Companies into RB&T will add approximately $700 million of assets under management. This acquisition is expected to close early in the fourth quarter of 2018.

Deposit service fees expanded 10% comparing the second quarter of 2018 to the same period of the prior year and expanded 13% when comparing the first half of 2018 to the same period of the prior year. This increase was primarily the result of the growth in deposits due to the acquisition of Guaranty Bank. Additionally, the Company continues its emphasis on shifting the mix of deposits from brokered and retail time deposits to non-maturity demand deposits across all its markets. With this continuing shift in mix, the Company has increased the number of demand deposit accounts, which tend to be lower in interest cost and higher in service fees. The Company plans to continue this shift in mix and to further focus on growing deposit service fees.

Gains on sales of residential real estate loans decreased 10% when comparing the second quarter of 2018 to the same period of the prior year and decreased 3% when comparing the first half of 2018 to the same period of the prior year. Overall, with the continued low interest rate environment, refinancing activity has slowed, as many of the Company's existing and prospective customers have already executed a refinancing. Therefore, this area has generally become a smaller contributor to overall noninterest income.

The Company's gains on the sale of government-guaranteed portions of loans for the second quarter of 2018 decreased 100% compared to the second quarter of 2017 and decreased 66% when comparing the first half of 2018 to the same period of the prior year. Given the nature of these gains, large fluctuations can occur from quarter-to-quarter and year-to-year. As one of its core strategies, the Company continues to leverage its expertise by taking advantage of programs offered by the SBA and the USDA. In the past several years, the Company's portfolio of government-guaranteed loans has grown as a direct result of the Company's strong expertise in SBA and USDA lending. In some cases, it is more beneficial for the Company to sell the government-guaranteed portion on the secondary market for a premium rather than retain the loans in the Company's portfolio. Sales activity for government-guaranteed portions of loans tends to fluctuate depending on the demand for loans that fit the criteria for the government guarantee. Further, the size of the transactions can vary and, as the gain is determined as a percentage of the guaranteed amount, the resulting gain on sale can vary. Lastly, a strategy for improved pricing is packaging loans together for sale. From time to time, the Company may execute on this strategy, which may delay the gains on sales of some loans to achieve better pricing. Recently, competitors have been offering SBA loan candidates traditional financing without the guarantee and the Company is not willing to relax structure for those lending opportunities.

As a result of the continued relatively low interest rate environment including a flat yield curve, the Company was able to execute numerous interest rate swaps on select commercial loans. The interest rate swaps allow the commercial borrowers to pay a fixed interest rate while the Company receives a variable interest rate as well as an upfront fee dependent upon the pricing. Management believes that these swaps help position the Company more favorably for rising rate environments. Management will continue to review opportunities to execute these swaps at all of its subsidiary banks, as the circumstances are appropriate for the borrower and the Company. An optimal interest rate swap candidate must be of a certain size and sophistication which can lead to volatility in activity from quarter to quarter. Swap fee income totaled $1.6 million for the second quarter of 2018, compared to $328 thousand for the second quarter of 2017. Swap fee income totaled $2.6 million for the first half of 2018 compared to $441 thousand in the first half of 2017. Future levels of swap fee income are also dependent upon prevailing interest rates.

Earnings on BOLI decreased 13% comparing the second quarter of 2018 to the first quarter of 2018 and decreased 12% comparing the first half of 2018 to the first half of 2017. There were no purchases of BOLI within the last 12 months. Notably, a small portion of the Company's BOLI is variable rate whereby the returns are determined by the performance of the equity market. Equity market performance accounted for the majority of the decrease in earnings on BOLI. Management intends to continue to review its BOLI investments to be consistent with policy and regulatory limits in conjunction with the rest of its earning assets in an effort to maximize returns while minimizing risk.

Debit card fees are the interchange fees paid on certain debit card customer transactions. Debit card fees increased 14% comparing the second quarter of 2018 to the second quarter of the prior year and increased 11% comparing the first half of 2018 to the first half of 2017. This increase was primarily related to the acquisition of Guaranty Bank in the fourth quarter of 2017. These fees can vary based on customer debit card usage, so fluctuations from period to period may occur. As an opportunity to maximize fees, the Company offers a retail deposit product with a higher interest rate that incentivizes debit card activity, which has been taken advantage of by the Company's customers.

Correspondent banking fees increased 6% comparing the second quarter of 2018 to the second quarter of the prior year and increased 7% comparing the first half of 2018 to the first half of 2017. Management will continue to evaluate earnings credit rates and the resulting impact on deposit balances and fees while balancing the ability to grow market share. Correspondent banking continues to be a core strategy for the Company, as this line of business provides a high level of deposits that can be used to fund loan growth as well as a steady source of fee income. The Company now serves approximately 192 banks in Iowa, Illinois and Wisconsin.

Other noninterest income increased 23% comparing the second quarter of 2018 to the second quarter of the prior year and increased 30% comparing the first half of 2018 to the first half of 2017. These increases were primarily driven by fluctuations in net gains recognized on the disposal of leased assets.

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MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS - continued

NONINTEREST EXPENSE

The following tables set forth the various categories of noninterest expense for the three and six months ended June 30, 2018 and 2017.

	Three Months Ended				
	June 30, 2018	June 30, 2017	$ Change	% Change	
Salaries and employee benefits	$ 15,804,016	$ 12,930,944	$ 2,873,072	22.2	%
Occupancy and equipment expense	3,132,658	2,698,336	434,322	16.1	
Professional and data processing fees	2,771,223	2,340,699	430,524	18.4	
Acquisition costs	413,602	—	413,602	100.0	
Post-acquisition compensation, transition and integration costs	165,314	—	165,314	100.0	
FDIC insurance, other insurance and regulatory fees	840,458	645,277	195,181	30.2	
Loan/lease expense	260,089	260,284	(195)	(0.1)	
Net cost of (income from) operations of other real estate	(70,190)	27,957	(98,147)	(351.1)	
Advertising and marketing	753,084	567,588	185,496	32.7	
Bank service charges	466,091	447,445	18,646	4.2	
Correspondent banking expense	204,337	201,693	2,644	1.3	
CDI amortization expense	304,551	230,867	73,684	31.9	
Other	1,324,590	1,053,539	271,051	25.7	
Total noninterest expense	$ 26,369,823	$ 21,404,629	$ 4,965,194	23.2	%

	Six Months Ended				
	June 30, 2018	June 30, 2017	$ Change	% Change	
Salaries and employee benefits	$ 31,781,991	$ 26,238,275	$ 5,543,716	21.1	%
Occupancy and equipment expense	6,198,469	5,200,555	997,914	19.2	
Professional and data processing fees	5,478,939	4,424,091	1,054,848	23.8	
Acquisition costs	506,141	—	506,141	100.0	
Post-acquisition compensation, transition and integration costs	165,314	—	165,314	100.0	
FDIC insurance, other insurance and regulatory fees	1,596,669	1,266,519	330,150	26.1	
Loan/lease expense	550,836	553,822	(2,986)	(0.5)	
Net cost of operations of other real estate	61,552	42,187	19,365	45.9	

Advertising and marketing	1,446,323	1,177,019	269,304	22.9	
Bank service charges	906,662	871,346	35,316	4.1	
Correspondent banking expense	409,091	400,044	9,047	2.3	
CDI amortization	609,102	461,733	147,369	31.9	
Other	2,522,231	2,042,155	480,076	23.5	
Total noninterest expense	$ 52,233,320	$ 42,677,746	$ 9,555,574	22.4	%

Management places a strong emphasis on overall cost containment and is committed to improving the Company's general efficiency. One-time charges relating to acquisitions are expected to impact expense throughout 2018.

Salaries and employee benefits, which is the largest component of noninterest expense, increased from the second quarter of 2017 to the second quarter of 2018 by 22%. This line item also increased 21% when comparing the first half of 2018 to the first half of 2017. This increase was primarily related to new hires, merit increases and the addition of the Guaranty Bank employees. To help support recent and expected growth, the Company is adding to operational infrastructure and investing in additional staffing both at the corporate level and at some of the bank charters. Some of these hires are opportunistic, as the Company takes advantage of strong talent in the marketplace as a result of ongoing industry consolidation.

Occupancy and equipment expense increased 16%, comparing the second quarter of 2018 to the same period of the prior year and increased 19% comparing the first half of 2018 to the same period of the prior year. The increased expense was primarily due to the addition of Guaranty Bank.

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Professional and data processing fees increased 18%, comparing the second quarter of 2018 to the same period in 2017 and increased 24% comparing the first half of 2018 to the same period of the prior year. This increased expense was partially due to the addition of Guaranty Bank. Additionally, legal expense was also elevated due to a legal matter at RB&T where two employees have been charged with wrongdoing in connection with an SBA loan application. The Company anticipates these legal expenses will continue to increase until the court proceedings are completed, which the Company expects to be in late 2018. Neither RB&T nor the Company have been charged in the case. Generally, professional and data processing fees can fluctuate depending on certain one-time project costs. Management will continue to focus on minimizing one-time costs and driving recurring costs down through contract renegotiation or managed reduction in activity where costs are determined on a usage basis.

Acquisition costs totaled $413 thousand for the second quarter of 2018 and $506 thousand for the first half of 2018. There were no acquisition costs in the first half of 2017. These costs were comprised primarily of legal, accounting and investment banking costs related to the acquisitions described in Note 10 to the Consolidated Financial Statements.

Post-acquisition costs totaled $165 thousand for the second quarter of 2018 and for the first half of 2018. These costs were comprised primarily of personnel costs, IT integration, and data conversion costs related to acquisitions.

FDIC insurance, other insurance and regulatory fee expense increased 30%, comparing the second quarter of 2018 to the second quarter of 2017 and increased 26% comparing the first half of 2018 to the same period of the prior year. The increase in expense was due to the acquisition of Guaranty Bank.

Loan/lease expense remained flat when comparing the second quarter of 2018 to the same quarter of 2017 as well as when comparing the first half of 2018 to the same period of the prior year. Generally, loan/lease expense has a direct relationship with the level of NPLs; however, it may deviate depending upon the individual NPLs.

Net cost of/income from operations of other real estate includes gains/losses on the sale of OREO, write-downs of OREO and all income/expenses associated with OREO. Net income from operations of other real estate totaled $70 thousand for the second quarter of 2018, compared to net costs of operations of $28 thousand for the second quarter of 2017. Net cost of operations of other real estate totaled $62 thousand for the first half of 2018 compared to $42 thousand for the same period of the prior year.

Advertising and marketing expense increased 33%, comparing the second quarter of 2018 to the second quarter of 2017 and increased 23% comparing the first half of 2018 to the same period of the prior year. The increase in expense was primarily due to the addition of Guaranty Bank.

Bank service charges, a large portion of which includes indirect costs incurred to provide services to QCBT's correspondent banking customer portfolio, increased 4% from the second quarter of 2017 to the second quarter of 2018 and increased 4%, comparing the first half of 2018 to the same period of the prior year. The increase was due, in large part, to the success QCBT has had in growing its correspondent banking customer portfolio. As transactions volumes continue to increase and the number of correspondent banking clients increases, the associated expenses will also increase.

Correspondent banking expense increased 1% when comparing the second quarter of 2018 to the second quarter of 2017 and increased 2% when comparing the first half of 2018 to the same period of the prior year. The increase was due to both increases in volume and in the number of correspondent banking clients. These are direct costs incurred to provide services to QCBT's correspondent banking customer portfolio, including safekeeping and cash management services.

CDI amortization expense increased 32% when comparing the second quarter of 2018 to the second quarter of 2017 and when comparing the first half of 2018 to the same period of the prior year. The increase was due to the acquisition of Guaranty Bank.

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Other noninterest expense was up 26% when comparing the second quarter of 2018 to the second quarter of 2017 and increased 24% when comparing the first half of 2018 to the same period of the prior year. Included in other noninterest expense are items such as subscriptions, sales and use tax and expenses related to wealth management. A portion of this increase is related to the addition of Guaranty Bank.

INCOME TAXES

In the second quarter of 2018, the Company incurred income tax expense of $1.9 million. During the first half of the year, the Company incurred income tax expense of $3.9 million. Following is a reconciliation of the expected income tax expense to the income tax expense included in the consolidated statements of income for the three and six months ended June 30, 2018 and 2017.

	For the Three Months Ended June 30,				For the Six Months Ended June 30,			
	2018		2017		2018		2017	
	Amount	% of Pretax Income	Amount	% of Pretax Income	Amount	% of Pretax Income	Amount	% of Pretax Income
mputed xpected" x expense	$ 2,588,503	21.0 %	$ 3,990,557	35.0 %	$ 5,222,119	21.0 %	$ 8,041,601	35.0 %
x exempt come, net	(956,089)	(7.8)	(1,433,903)	(12.6)	(1,899,190)	(7.6)	(2,739,330)	(11.9)
nk-owned e urance	(83,848)	(0.7)	(160,775)	(1.4)	(171,625)	(0.7)	(325,166)	(1.4)
te come es, net of deral nefit, rrent year	557,656	4.5	394,410	3.5	1,109,124	4.5	802,735	3.5
cess tax nefit on ck tions ercised d tricted ck ards sted	(200,644)	(1.6)	(89,545)	(0.8)	(333,005)	(1.3)	(622,867)	(2.7)

her	(24,759)	(0.1)	(65,168)	(0.6)	(55,534)	(0.3)	(131,951)	(0.6)
deral and te income expense	$ 1,880,819	15.3 %	$ 2,635,576	23.1 %	$ 3,871,889	15.6 %	$ 5,025,022	21.9 %

The effective tax rate for the quarter ended June 30, 2018 was 15.3% which was a 7.8% decrease from the effective tax rate of 23.1% for the quarter ended June 30, 2017. The effective tax rate for the six months ended June 30, 2018 was 15.6%, which was a decrease over the effective tax rate of 21.9% for the six months ended June 30, 2017. The Tax Act was enacted on December 22, 2017 and was effective January 1, 2018 reducing the federal corporate tax rate from 35% to 21%.

FINANCIAL CONDITION

Following is a table that represents the major categories of the Company's balance sheet.

	As of June 30, 2018 (dollars in thousands)		March 31, 2018		December 31, 2017		June 30, 2017	
	Amount	%	Amount	%	Amount	%	Amount	%
Cash and due from banks	$ 69,069	2 %	$ 61,846	2 %	$ 75,722	2 %	$ 77,161	2 %
Federal funds sold and interest-bearing deposits	51,667	1 %	59,557	1 %	85,962	2 %	72,354	2 %
Securities	657,997	16 %	638,229	16 %	652,382	16 %	593,485	17 %
Net loans/leases	3,077,247	75 %	3,018,370	75 %	2,930,130	74 %	2,520,209	73 %
Other assets	250,903	6 %	248,312	6 %	238,469	6 %	193,978	6 %
Total assets	$ 4,106,883	100 %	$ 4,026,314	100 %	$ 3,982,665	100 %	$ 3,457,187	100 %
Total deposits	$ 3,298,276	81 %	$ 3,280,001	82 %	$ 3,266,655	82 %	$ 2,870,234	83 %
Total borrowings	380,392	9 %	334,802	8 %	309,480	8 %	230,264	7 %
Other liabilities	58,627	1 %	51,083	1 %	53,243	1 %	51,606	1 %
Total stockholders' equity	369,588	9 %	360,428	9 %	353,287	9 %	305,083	9 %
Total liabilities and stockholders' equity	$ 4,106,883	100 %	$ 4,026,314	100 %	$ 3,982,665	100 %	$ 3,457,187	100 %

During the second quarter of 2018, the Company's total assets increased $80.6 million, or 2%, to a total of $4.1 billion. Net loans/leases grew $58.9 million. This loan and lease growth was funded by deposits, which increased $18.3 million in the second quarter of 2018, and borrowings, which increased $45.6 million in the second quarter of 2018. Stockholders' equity increased $9.2 million, or 3%, in the current quarter due to net retained income.

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INVESTMENT SECURITIES

The composition of the Company's securities portfolio is managed to meet liquidity needs while prioritizing the impact on interest rate risk and maximizing return, while minimizing credit risk. Over the past five years, the Company has further diversified the portfolio by decreasing U.S government sponsored agency securities, while increasing residential mortgage-backed and related securities and tax-exempt municipal securities. Of the latter, the large majority are privately placed tax-exempt debt issuances by municipalities located in the Midwest (with some in or near the Company's existing markets) and require a thorough underwriting process before investment.

Following is a breakdown of the Company's securities portfolio by type, the percentage of unrealized gains (losses) to carrying value on the total portfolio, and the portfolio duration:

	As of June 30, 2018		March 31, 2018		December 31, 2017		June 30, 2017	
	Amount	%	Amount	%	Amount	%	Amount	%
	(dollars in thousands)							
U.S. govt. sponsored agency securities	$ 35,667	5 %	$ 36,868	6 %	$ 38,097	6 %	$ 41,944	7 %
Municipal securities	458,510	70 %	438,736	69 %	445,049	68 %	381,254	64 %
Residential mortgage-backed and related securities	158,534	24 %	157,289	24 %	163,301	25 %	164,415	28 %
Other securities	5,286	1 %	5,336	1 %	5,935	1 %	5,872	1 %
	$ 657,997	100 %	$ 638,229	100 %	$ 652,382	100 %	$ 593,485	100 %
Securities as a % of Total Assets	16.02 %		15.85 %		16.38 %		17.17 %	
Net Unrealized Losses as a % of Amortized Cost	(1.58) %		(1.01) %		(0.13) %		(0.33) %	
Duration (in years)	7.0		6.9		7.0		6.3	
Quarterly Yield on Investment Securities (TEY)	3.56 %		3.65 %		3.82 %		3.76 %	
Quarterly Yield on Investment Securities	3.02 %		3.03 %		2.77 %		2.75 %	

(GAAP)

Management monitors the level of unrealized gains/losses including performing quarterly reviews of individual securities for evidence of OTTI. Management identified no OTTI in any of the periods presented.

The duration of the securities portfolio shortened modestly with the TEY on the portfolio decreasing 26 bps in the first half of 2018; however, excluding the tax benefit and the related variance due to the lower tax rate, the portfolio yield expanded 25 basis points.

The Company has not invested in private mortgage-backed securities or pooled trust preferred securities. Additionally, the Company has not invested in the types of securities subject to the Volcker Rule (a provision of the Dodd-Frank Act).

See Note 2 to the Consolidated Financial Statements for additional information regarding the Company's investment securities.

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LOANS/LEASES

Total loans/leases grew 7.8% on an annualized basis during the second quarter of 2018. The mix of the loan/lease types within the Company's loan/lease portfolio is presented in the following table.

	As of June 30, 2018		March 31, 2018		December 31, 2017		June 30, 2017	
	Amount	%	Amount	%	Amount	%	Amount	%
	(dollars in thousands)							
C&I loans	$ 1,273,000	42 %	$ 1,201,087	39 %	$ 1,134,516	38 %	$ 942,538	37 %
CRE loans	1,349,319	43 %	1,357,703	45 %	1,303,492	44 %	1,131,906	45 %
Direct financing leases	133,196	4 %	137,614	5 %	141,448	5 %	153,337	6 %
Residential real estate loans	257,434	8 %	254,484	8 %	258,646	9 %	233,871	9 %
Installment and other consumer loans	92,952	3 %	95,912	3 %	118,611	4 %	84,047	3 %
Total loans/leases	$ 3,105,901	100 %	$ 3,046,800	100 %	$ 2,956,713	100 %	$ 2,545,699	100 %
Plus deferred loan/lease origination costs, net of fees	8,891		8,103		7,773		7,867	
Less allowance	(37,545)		(36,533)		(34,356)		(33,357)	
Net loans/leases	$ 3,077,247		$ 3,018,370		$ 2,930,130		$ 2,520,209	

As CRE loans have historically been the Company's largest portfolio segment, management places a strong emphasis on monitoring the composition of the Company's CRE loan portfolio. For example, management tracks the level of owner-occupied CRE loans relative to non owner-occupied loans. Owner-occupied loans are generally considered to have less risk. As of June 30, 2018 and December 31, 2017, approximately 26% of the CRE loan portfolio was owner-occupied.

Over the past several quarters, the Company has been successful in shifting the mix of its commercial loan portfolio by adding more C&I loans. C&I loans grew $71.9 million in the current quarter.

A syndicated loan is a commercial loan provided by a group of lenders and is structured, arranged and administered by one or several commercial or investment banks known as arrangers. The nationally syndicated loans invested in by the Company consist of fully funded, highly liquid term loans for which there is a liquid secondary market. As of June 30, 2018 and December 31, 2017, the amount of nationally syndicated loans totaled $38.6 million and $51.2 million, respectively.

Following is a listing of significant industries within the Company's CRE loan portfolio:

	As of June 30, 2018		As of March 31, 2018		As of December 31, 2017		As of June 30, 2017	
	Amount	%	Amount	%	Amount	%	Amount	%
	(dollars in thousands)							
Lessors of Nonresidential Buildings	$ 439,067	33 %	$ 435,919	32 %	$ 388,648	30 %	$ 344,747	30 %
Lessors of Residential Buildings	230,187	17 %	221,978	16 %	199,047	15 %	159,370	14 %
Hotels	73,335	5 %	70,887	5 %	70,447	5 %	39,881	4 %
Nonresidential Property Managers	55,979	4 %	56,572	4 %	51,621	4 %	52,947	5 %
Land Subdivision	39,883	3 %	45,356	3 %	44,192	3 %	46,117	4 %
New Housing For-Sale Builders	38,392	3 %	52,951	4 %	61,480	5 %	52,277	5 %
Nursing Care Facilities	37,417	3 %	38,830	3 %	47,008	4 %	33,607	3 %
Lessors of Other Real Estate Property	28,149	2 %	31,121	2 %	29,078	2 %	20,932	2 %
Other *	406,910	30 %	404,089	30 %	411,971	32 %	382,028	33 %
Total CRE Loans	$ 1,349,319	100 %	$ 1,357,703	100 %	$ 1,303,492	100 %	$ 1,131,906	100 %

* “Other” consists of all other industries. None of these had concentrations greater than $27.0 million, or approximately 2% of total CRE loans in the most recent period presented.

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The Company's residential real estate loan portfolio includes the following:

- Certain loans that do not meet the criteria for sale into the secondary market. These are often structured as adjustable rate mortgages with maturities ranging from three to seven years to avoid the long-term interest rate risk.
- A limited amount of 15 year and 20 year fixed rate residential real estate loans that meet certain credit guidelines.

The remaining residential real estate loans originated by the Company were sold on the secondary market to avoid the interest rate risk associated with longer term fixed rate loans. Loans originated for this purpose were classified as held for sale and are included in the residential real estate loans above. The Company has not originated any subprime, Alt-A, no documentation, or stated income residential real estate loans throughout its history.

Following is a listing of significant equipment types within the m2 loan and lease portfolio:

	As of June 30, 2018		As of March 31, 2018		As of December 31, 2017		As of June 30, 2017	
	Amount	%	Amount	%	Amount	%	Amount	%
	(dollars in thousands)							
Trucks, Vans and Vocational Vehicles	$ 35,814	15 %	$ 28,219	13 %	$ 19,927	9 %	$ 16,679	8 %
Construction - General	18,494	8 %	18,067	8 %	18,705	9 %	15,207	7 %
Manufacturing - General	16,794	7 %	16,624	7 %	16,571	8 %	19,092	9 %
Food Processing Equipment	14,377	6 %	13,270	6 %	12,965	6 %	13,754	7 %
Marine - Travelifts	12,875	6 %	12,843	6 %	10,802	5 %	12,497	6 %
Computer Hardware	10,141	4 %	10,694	5 %	11,340	5 %	9,821	5 %
Trailers	10,137	4 %	9,161	4 %	8,983	4 %	9,611	5 %
Miscellaneous Equipment	7,032	3 %	6,459	3 %	6,644	3 %	5,126	2 %
Restaurant	6,509	3 %	6,844	3 %	7,107	3 %	7,238	3 %
Other *	101,124	44 %	101,473	45 %	102,192	48 %	105,228	48 %
Total m2 loans and leases	$ 233,297	100 %	$ 223,654	100 %	$ 215,236	100 %	$ 214,253	100 %

* “Other” consists of all other equipment types. None of these had concentrations greater than 3% of total m2 loan and lease portfolio in the most recent period presented.

See Note 3 to the Consolidated Financial Statements for additional information regarding the Company's loan and lease portfolio.

ALLOWANCE FOR ESTIMATED LOSSES ON LOANS/LEASES

Changes in the allowance for the three and six months ended June 30, 2018 and 2017 are presented as follows:

	Three Months Ended		Six Months Ended	
	June 30, 2018	June 30, 2017	June 30, 2018	June 30, 2017
	(dollars in thousands)		(dollars in thousands)	
Balance, beginning	$ 36,533	$ 32,059	$ 34,356	$ 30,757
Provisions charged to expense	2,301	2,023	4,841	4,128
Loans/leases charged off	(1,524)	(851)	(1,961)	(1,743)
Recoveries on loans/leases previously charged off	235	126	309	215
Balance, ending	$ 37,545	$ 33,357	$ 37,545	$ 33,357

The allowance was determined based on factors that included the overall composition of the loan/lease portfolio, types of loans/leases, past loss experience, loan/lease delinquencies, potential substandard and doubtful credits, economic conditions, collateral positions, governmental guarantees and other factors that, in management's judgment, deserved evaluation. To ensure that an adequate allowance was maintained, provisions were made based on a number of factors,

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including the increase in loans/leases and a detailed analysis of the loan/lease portfolio. The loan/lease portfolio is reviewed and analyzed monthly with specific detailed reviews completed on all loans risk-rated worse than "fair quality", as described in Note 1 to the Consolidated Financial Statements contained in the Company's Annual Report on Form 10 K for the year ended December 31, 2017, and carrying aggregate exposure in excess of $250 thousand. The adequacy of the allowance is monitored by the loan review staff and reported to management and the board of directors.

The Company's levels of criticized and classified loans are reported in the following table.

Internally Assigned Risk Rating *	As of June 30, 2018	March 31, 2018	December 31, 2017	June 30, 2017
	(dollars in thousands)			
Special Mention (Rating 6)	$ 44,202	$ 42,926	$ 31,024	$ 27,737
Substandard (Rating 7)	42,492	39,815	43,435	45,290
Doubtful (Rating 8)	—	—	271	—
	$ 86,694	$ 82,741	$ 74,730	$ 73,027
Criticized Loans **	$ 86,694	$ 82,741	$ 74,730	$ 73,027
Classified Loans ***	$ 42,492	$ 39,815	$ 43,706	$ 45,290
Criticized Loans as a % of Total Loans/Leases	2.79 %	2.79 %	2.52 %	2.86 %
Classified Loans as a % of Total Loans/Leases	1.37 %	1.34 %	1.47 %	1.77 %

* Amounts above include the government guaranteed portion, if any. For the calculation of allowance, the Company assigns internal risk ratings of Pass (Rating 2) for the government guaranteed portion.

** Criticized loans are defined as commercial and industrial and commercial real estate loans with internally assigned risk ratings of 6, 7, or 8, regardless of performance.

*** Classified loans are defined as commercial and industrial and commercial real estate loans with internally assigned risk ratings of 7 or 8, regardless of performance.

The Company experienced a 7% increase in classified loans during the second quarter of 2018. Criticized loans increased 5% during the same period. The Company experienced a decrease of 3% in classified loans during the first six months of 2018. Criticized loans increased 16% during the same period. The Company continues its strong focus on improving credit quality in an effort to limit NPLs.

As of

	June 30, 2018		March 31, 2018		December 31, 2017		June 30, 2017	
Allowance / Gross Loans/Leases	1.21	%	1.20	%	1.16	%	1.31	%
Allowance / NPLs	270.09	%	202.11	%	184.28	%	162.27	%

Although management believes that the allowance at June 30, 2018 was at a level adequate to absorb losses on existing loans/leases, there can be no assurance that such losses will not exceed the estimated amounts or that the Company will not be required to make additional provisions in the future. Unpredictable future events could adversely affect cash flows for both commercial and individual borrowers, which could cause the Company to experience increases in problem assets, delinquencies and losses on loans/leases, and require further increases in the provision. Asset quality is a priority for the Company and its subsidiaries. The ability to grow profitably is in part dependent upon the ability to maintain that quality. The Company continually focuses efforts at its subsidiary banks and leasing company with the intention to improve the overall quality of the Company's loan/lease portfolio.

See Note 3 to the Consolidated Financial Statements for additional information regarding the Company's allowance.

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NONPERFORMING ASSETS

The table below presents the amount of NPAs and related ratios.

	As of June 30, 2018	As of March 31, 2018	As of December 31, 2017	As of June 30, 2017
	(dollars in thousands)			
Nonaccrual loans/leases (1) (2)	$ 12,554	$ 12,759	$ 11,441	$ 13,217
Accruing loans/leases past due 90 days or more	20	41	89	424
TDRs - accruing	1,327	5,276	7,113	6,915
Total NPLs	13,901	18,076	18,643	20,556
OREO	12,750	12,750	13,558	5,174
Other repossessed assets	150	200	80	123
Total NPAs	$ 26,801	$ 31,026	$ 32,281	$ 25,853
NPLs to total loans/leases	0.45 %	0.59 %	0.63 %	0.80 %
NPAs to total loans/leases plus repossessed property	0.86 %	1.01 %	1.08 %	1.01 %
NPAs to total assets	0.65 %	0.77 %	0.81 %	0.75 %

(1) Includes government guaranteed portion of loans, as applicable.
(2) Includes TDRs of $1.8 million at June 30, 2018, $2.6 million at March 31, 2018, $2.3 million at December 31, 2017, and $2.2 million at June 30, 2017.

NPAs at June 30, 2018 were $26.8 million, down $4.2 million from March 31, 2018 and up $948 thousand from June 30, 2017. The decrease in the second quarter of 2018 was due to one large loan that was upgraded and taken out of TDR status.

The ratio of NPAs to total assets was 0.65% at June 30, 2018, down from 0.77% at March 31, 2018 and down from 0.75% at June 30, 2017.

The large majority of the NPAs consist of nonaccrual loans/leases, accruing TDRs, and OREO. For nonaccrual loans/leases and accruing TDRs, management has thoroughly reviewed these loans/leases and has provided specific allowances as appropriate.

OREO is carried at the lower of carrying amount or fair value less costs to sell.

The Company's lending/leasing practices remain unchanged and asset quality remains a priority for management.

DEPOSITS

Deposits increased $18.3 million during the second quarter of 2018. The table below presents the composition of the Company's deposit portfolio.

	As of June 30, 2018		March 31, 2018		December 31, 2017		June 30, 2017	
	Amount	%	Amount	%	Amount	%	Amount	%
	(dollars in thousands)							
Noninterest bearing demand deposits	$ 746,822	23 %	$ 784,815	24 %	$ 789,548	24 %	$ 760,625	27 %
Interest bearing demand deposits	1,865,382	57 %	1,789,019	55 %	1,855,893	57 %	1,526,103	52 %
Time deposits	519,999	16 %	496,644	15 %	516,058	16 %	478,580	17 %
Brokered deposits	166,073	5 %	209,523	6 %	105,156	3 %	104,926	4 %
	$ 3,298,276	100 %	$ 3,280,001	100				